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FACULTY OF ECONOMICS

DEPARTMENT OF FINANCE

Hodnocení finanční výkonnosti společnosti IKEA

Evaluation of Financial Performance of IKEA Company

Student: Zhang Yichen

Supervisor of the bachelor thesis: Ing. Kateřina Zelinková

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Student: **Yichen Zhang**  
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### Description:

1. Introduction  
2. Description of the Financial Analysis Methodology  
3. Profile of IKEA Company  
4. Financial Analysis of IKEA Company  
5. Conclusion  
Bibliography  
List of Abbreviations  
Declaration of Utilization of Results from the Bachelor Thesis  
List of Annexes  
Annexes

### References:


BRIGHAM, Eugene F. and Michael C. EHRHARDT. *Financial Management: Theory and Practice*. 13th ed. Mason: South-Western Cengage Learning, 2011. ISBN 978-1-4390-7810-5.  
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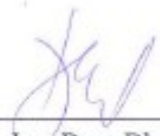
Supervisor: **Ing. Kateřina Zelinková**

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Ing. Iveta Ratmanová, Ph.D.  
Head of Department



  
prof. Dr. Ing. Dana Dluhašová  
Dean of Faculty

“Herewith I declare that I elaborated the entire thesis, including all annexes, independently.”

In Ostrava 6. May 2015

.....YICHEN ZHANG.....  
Student's name and surname

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## **1. Introduction**

IKEA Company was founded in Sweden in 1943, it is one of the most successful companies and it is the biggest furnishing company in the world, as a worldwide company, its development reflects the general rule of multinationals' growth after the World War II, we can follow the golden rule of international strategy in the world and find the reason of its development during a period, so we choose to analyze the financial situation of IKEA, because it has typicality in the industry.

The goal of submitted bachelor thesis is to assess the financial performance of IKEA Company during 2010 to 2013 periods.

Financial analysis is the core part in this thesis, for a company, it is very necessary to use the methods to examine the financial health of it. In the process of the financial analysis, we can clearly know more technical information about the company. We need to use the different tools of financial analysis based on the collected data to calculate and assess the performance, then we can make a basic conclusion about its financial health. Using these methods, we can know what and why the performance that company has, so then we can clearly know what to be next and give advices for the company in order to have a better development.

This bachelor thesis can be divided into five parts. The first part is the introduction and the final part is the conclusion, we can give some advises to the company. In the second part, we introduce the basic financial analysis methodologies, we describe the financial statements and financial analysis methods, we found the data and make the financial statements, then use the relative data and apply them for these methods, they are using for examine the performance of the IKEA Company. The financial methods include the common size analysis, the trend analysis, the financial ratio analysis and the pyramidal decomposition analysis. So we can use these methods to evaluate and make a conclusion about the financial health of IKEA Company, we can find its trend in the future, it is very necessary to this analysis no matter for the company itself or for the investors or for the financial analysts.

In the third part, we introduce the profile about the IKEA Company, firstly, we introduce the basic information about the company, describe its basic operation principle and its

characteristics. Next we introduce the company based on its history from 1943 to now, we can see and track the way that how the company developed and learn its successful way from it. Then we introduce the business strategy of the company. We describe its unique business management structure- Stichting INGKA Foundation and describe more details of the reasons that made it successful in four parts.

In the fourth part, we put the theory in the second part into practice. Firstly, we use the common size analysis and the trend analysis to assess the basic situation of financial statements of the IKEA Company. Next, we use the financial ratios include profitability ratio, liquidity ratio, solvency ratio and activity ratio. Lastly, we use the pyramidal decomposition ratio of return on equity, we can find the key information from it, this method is complicated, we need to decompose and find the components of return on equity then find out which factors has the biggest influence on it. After that, we use the methods of gradual changes and logarithmic methods and functional decomposition method, then we compare the results from these three methods. By using these methods, we can find out the reason that affects the financial health of the company and deal with them in order to have a better development in the future.



## 2 Description of the Financial Analysis Methodology

In this chapter, we will introduce the basic financial analysis methodology. “The financial analysis of a company is a process of selecting, evaluating, and interpreting financial data, along with other pertinent information, in order to formulate an assessment of the company’s present and future financial condition and performance”<sup>1</sup>. The financial analyst need to collect and select the useful information to analyze and explain it, their task is to make judgements on the current and future condition and the financial performance of the company.

### 2.1 Financial Statement

Financial statement is the main part of the financial report. The accounting information that it provides has very important role, it is closely connected with the companies’ financial stability and profitability. The financial figures in financial statement reflect the current condition and business strategies in companies. No matter individuals or banks, they all need to find the results from the financial statements and make decisions.

Knowing the basic information about the financial statement analysis, we should know the framework about it. As financial analysts, they need to ensure their purpose and evaluate the condition of analysis, and then they need to collect data and process it, after they can analyze the processed data and develop and make a summary

#### 2.1.1 Balance Sheet

Balance Sheet, also known as the statement of financial position (SOFPP), it represents businesses’ financial situation (i.e., status of assets, liabilities and owners’ equity) in certain date (usually for the accounting period) of the main financial statements. Usually analysts will start to analysis a company’s financial condition according to the balance sheet. It shows the interest in possession or control of economic resources at a certain date, the owners claim the obligations for the net assets. *It normally provides information about the future earnings capacity of a company’s assets as well as an indication of cash flows that may come from receivables and inventories.*

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<sup>1</sup> Robinson, Thomas R. et al. *International Financial Statement Analysis*. 2nd edition. New York: John Wiley and Sons, 2012. ISBN: 978-0-470-91662-9

The basic equation of accounting is

$$A=L+E \quad (2.1)$$

where  $A$  is assets,  $L$  is liabilities,  $E$  is shareholder's equity.

Assets represent the economic resources of a company, they are generated either by purchase (investing activities), business activities (operating activities) or financing activities, including fixed assets, current assets and depreciation. Fixed assets like long-term assets, which are relatively low liquidity and have relatively long life, they are usually divided into tangible assets (land, equipment, etc.), intangible assets (trademark, patents, etc.). Current assets like short-term assets that have high liquidity because it can be relatively quickly converted into cash and have relatively short life, they can be divided into receivables, inventories and cash or cash equivalents like short-term tradable securities. There are some typical assets shown in the balance sheet include *cash and cash equivalents, inventories, trade and other receivables, prepaid expenses, financial assets, deferred tax assets, property, plant and equipment, intangible assets, investments accounted for using the equity method, natural resource assets, and assets held for sale.*

There is one important factor in asset we need to know that is inventories, it measures the lower of cost or net realized value. Generally, we need to take these following amount into consideration about measuring the inventory costs: Standard cost and the retail method. The standard cost need to be reviewed at regular intervals in order to ensure its actual costs, we should take the normal levels of materials, labor and actual capacity into account. About the retail method, the value of sales is decreased by the gross margin to calculate the cost, we need to consider about the impact of marked-down prices.

Liabilities present the obligation that a company needs to pay back from its past events, it shows the outflow of business benefits from the entity. It can be described as the probable responsibilities that need to provide services to other entities in the future according to its past transactions or events. There are two kinds of conditions that we need to know, firstly, if the amounts received but it has not been reported as revenues or income in income statement, we need to repaid it, like notes payable, it is evidence of loan agreement that amounts of money owed by creditors of a business as a result of borrowing; Secondly, if the amounts received

which have been reported as the expenses in income statement but didn't repaid, like tax payable, There are some typical liabilities shown in the balance sheet: *Bank borrowing/notes payable, trade and other payable, provisions, unearned revenues, financial liabilities, accrued liabilities, deferred tax liabilities.*

Equity is commonly known as the shareholders' equity or owner's equity, it presents the portion, which belongs to the shareholders, or owners in business activities, it equals to the assets minus the liabilities of a company, we can know it from the formula (2.1). It can be viewed as balancing amount, we need to take the assets and liabilities into account. It is increased by the owners or by profits including gain during a year and decreased by losses in the form of dividends. The amount of capital can affect the competition of a company, it is because that the shareholders expect to get return on their equity, and it is depends on the pricing of company products, the perspective of the market can also influence the level of capital. If a company faces the shortage of equity capital, or there is another condition if the cost of capital is high, so the company takes the risk of losing business to its competitors. The equity capital can provide the stability and decrease the risk of losses, so it is very necessary to provide a protection for creditors to ensure liquidity. There are three important characteristics about the capital in a company, firstly, *it should be permanent*; Secondly, *it should not impose mandatory fixed charges against earning in the case of banks*; Thirdly, *it should allow for legal subordination to the rights of creditors.*

There are some typical equity information shown in the balance sheet: *Issued capital and paid-in capital attributable to equity holders of the parent, earnings retained in the company, minority interest and presented within equity, parent shareholders' equity.*

Here is an example about balance sheet.

**Table 2.1 Balance sheet**

<b>Assets</b>		<b>Liabilities</b>	
Cash	\$375	Notes Payable	\$0
Accts. Receivable	\$0	Accts. Payable	\$0
		Tot. Liabilities	\$0
<b>Inventory</b>		<b>Owner's Equity</b>	
Raw Materails	\$0	Orig. Investment	\$100
Finished Goods	\$0	Retained Earnings	\$220
		Earnings Wk. Ending	\$95
Prepaid Expenses	\$40	Tot. Owner's Equity	\$415
<b>Total Assets</b>	<b>\$415</b>	<b>Liabilities &amp; Owner Equity</b>	<b>\$415</b>

Source: <http://www.newthinktank.com/2010/10/the-balance-sheet-pt-2/>

We see from this table that the total asset is equal to the liabilities & owner equity, is \$415.

So we can clearly see the basic application in the balanced sheet from this table. Liabilities refer to the obligation of a company, it shows how much money that the company need to pay to like lenders, employees and so on, including current liabilities and long-term debt.

Owner's equity can also be called net-worth, it shows the residual claim of resources, including retained earnings and capital stock.

Balance sheet has important significance. It is the most important companies' accounting reporting system in the financial statements, the information that it provides has important effect for the enterprise management department, the higher authorities, investors, banks and other financial institutions, also the tax department.

It can explain, evaluate and predict the short-term and long-term solvency of the enterprise and capital structure. The solvency is mainly reflected by the liquidity of corporate assets and liabilities. Capital structure usually refers to the relationship about the total corporate capital structure debt and equity in owner's equity and liabilities in current liabilities and long-term liabilities, the equity invested capital and retained earnings or common shares and preferred shares. Also it can explain, evaluate and predict the companies' financial flexibility, performance and help the management department to make right business decisions.

However we need to aware of that the balance sheet does have limitations, especially when connecting with how the assets and liabilities are measure. The readers should have ability to make appropriate use of it by understanding how a balance sheet is constructed and how it should be calculated and analyzed.

### 2.1.2 Income Statement

Income statement also called profit and loss statement, which indicates the amount of profit generated by a company over a certain accounting period, often a year. And it also presents the information about its financial results of a company's business activities over a period of time. The operating results can appear to be both profitable and loss. The basic equation of accounting is

$$R-C=I \quad (2.2)$$

where  $R$  is revenue,  $C$  is cost,  $I$  is income.

Revenues represent the inflows of economic resource of the company, *it refers to amounts charged for the delivery of goods or services in the ordinary activities of a business*. Costs are the outflows of economic resources in liabilities. Income represents the difference between the price at which goods or services are provided to customers and expenses which need to provide good and services.

There are two main subtotals are calculated:

- operating activity,
- financing activity.

#### Operating activity

It's calculated as a difference between the sum of operating revenues and operating costs. Sometimes it can be called as operating profit before interest and taxes- *EBIT*. The operating revenues mean the revenues from the sale of the goods and services. The operating costs mean the cost connected with generating operating revenues like *electricity consumption, raw*

*material consumption, costs of good sold, depreciations, salaries and wages paid to employees, administrative costs and other operating costs.*<sup>2</sup>

### **Financing activity**

It's calculated as a difference between the sum of financing revenues and financing costs. Financing revenues include interests received, revenues from owned securities like dividends received, coupon received and so on. Financing costs include interests paid, coupon paid (if bonds are issued) and so on. The sum of operating and financing income equal profit before tax (*EBT*), then the company's tax (*T*) is calculated by applying corporate tax rate (*t*),

$$T = EBT \cdot t \quad (2.3)$$

so the resulting number that the profit after tax (*EAT*), net income equals to revenues minus costs.

Through the income statement, firstly, it can be regarded as the reason for the distribution about the operating results, because income statements reflects the operating income, operating costs and business taxes, fees and operating income of a company in a certain period during the project then calculate the final result of the profit integrated indicators. Secondly, income statement can reflect all aspects of production and business activities, it can contribute to the evaluation about the personal enterprise management of job performance. Thirdly, income statement can be used to analyze the profitability of the company and predict the future cash flow about the company.

We can see a simple example of an income statement.

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<sup>2</sup> Robinson, Thomas R. et al. *International Financial Statement Analysis*. 2nd edition. New York: John Wiley and Sons, 2012. ISBN: 978-0-470-91662-9

**Table 2.2 Income statement**

Income Statement For the Three Months Ending March 31, 2006		
	Year to Date	
Revenues		
Landscaping Fees	\$ 20,075.00	99.50
Finance Charge Income	100.00	0.50
Total Revenues	20,175.00	100.00
Cost of Sales		
Total Cost of Sales	0.00	0.00
Gross Profit	20,175.00	100.00
Expenses		
Auto Expense	2,200.00	10.90
Commissions and Fees Exp	6,000.00	29.74
Dues and Subscriptions Exp	600.00	2.97
Insurance Expense	250.00	1.24
Total Expenses	9,050.00	44.86
Net Income	\$ 11,125.00	55.14

Source: <https://www.e-economic.com/accountingsoftware/accounting-words/income-statement>

From this part, we can make a conclusion that the income statement presents the revenue, expenses, and net income, we can measure how much the revenue that the company earned during a period and what the costs in connected with the revenue. Also the income statement presents the part of gross profit, it equals the revenue minus the cost of goods or services are sold. The results of calculation about the revenue may be different by an analyst according to the different methods. In order to assess a company's future earnings, we need to separate some items which are less to continue to happen, so the financial analyst need to distinguish from them.

### 2.1.3 Cash Flow

Though we don't use the cash flow in practical part because of the limit of collecting the relative sources, as one of the important statements, it's necessary to introduce the basic principle about it in this part.

Cash flow statement provides the information about the company's cash inflows and outflows during a period, often a year, it shows the connection between the ending cash balance with the

beginning balance which shown on the company's balance sheet, the information about the cash provided by the cash statement also with accrual-based information from the income statement, so we can find that *the cash flow statement is linked to the company's income statement and comparative balance sheets and it is constructed from the data on those statements*. Cash inflows mean the amount of money received during a period, outflow mean the amount of money spent as cash receipts during a period.

According to its use, it can be classified into three categories: operating, investing and financing activities.

In operating activities, it includes inflows and outflows from day-to-day company's activities. Cash inflows include cash sales of goods, products or services, collection of receivables and so on. Cash outflows include Cash payment for inventory, salary and wages payment, taxes, paying payables, etc.

In investing activities, it includes inflows and outflows as the result of selling and purchasing of investments, the investments include tangible assets (property, equipment, etc.), intangible assets (patents, trademark, etc.) and long-term investments in the shares and bonds.

In financing activities, it includes inflows and outflows from obtaining and repaying capital (equity and long-term debt). Cash inflows mean the cash from issuing shares (common and preferred) or bonds and cash from credits and borrowings. Cash outflows have three parts include paying out dividends, repaying bonds and repay credits and borrowings.

The total cash flow equals to cash flow from operating activities add to cash flow from investing activities add to cash flow from financing.

Through the cash flow statement, it makes up for the lack of balance information, it's easier to facilitate enterprise assessment from the perspective of cash flow and it can reflect the ability about raising money and converting to cash of the company



**Table 2.3 Cash flow**

<b>Cash Flow Statement</b> <b>Company XYZ</b> <b>FY Ended 31 Dec 2003</b>	
all figures in USD	
<b>Cash Flow From Operations</b>	
Net Earnings	2,000,000
<i>Additions to Cash</i>	
Depreciation	10,000
Decrease in Accounts Receivable	15,000
Increase in Accounts Payable	15,000
Increase in Taxes Payable	2,000
<i>Subtractions From Cash</i>	
Increase in Inventory	(30,000)
<b>Net Cash from Operations</b>	<b>2,012,000</b>
<b>Cash Flow From Investing</b>	
Equipment	(500,000)
<b>Cash Flow From Financing</b>	
Notes Payable	10,000
<b>Cash Flow for FY Ended 31 Dec 2003</b>	<b>1,522,000</b>

Source: <http://www.investopedia.com/articles/04/033104.asp>

We can see that the total cash flow in 2003 was \$1,522,000, it shows a good sign for investors.

## 2.2 The Methods of Financial Analysis

Financial analysis is the process of selecting, evaluation and interpreting the financial data. We can evaluate company's operations, management and credit policies, etc. The aim of the analysis is to formulate the assessment of the company's present and future financial position also for its health. Besides the financial statement data, economic data and market data, we all need to evaluate the events that can help to explain the company's present condition and may using it in future prospects. In this part, we will introduce the tools of the financial analysis, these tools include common size analysis, trend analysis, financial ratio analysis, pyramidal decomposition analysis.

### 2.2.1 Common Size analysis

Common size analysis is the analysis of the financial statement data and examine their changes over the time. The aim is to identify the trend and spot the major difference of the company, it's a very useful way. We can easily compare the changes whatever in one company or in two or more companies. Based on the changes, we can recognize the average level on one industry.

There are two types of this analysis: horizontal common size analysis and vertical common size analysis. The most common is vertical common-size analysis, we can compare the amounts in a given period based on a benchmark item in the same year. For the income statement, the benchmark is revenues; for the balance sheet, the benchmark is the total assets. We can use these methods on financial statements.

Horizontal common size analysis is the analysis of the change of financial statements data over the time or the changes with respect to a given period as a benchmark. There are two methods to calculate this analysis that include comparative financial statements and index trend analysis. In comparative financial statements method, the benchmark means each previous year, but index trend analysis use a fixed benchmark. We usually use the whole statement to explain the data.

Vertical common-size analysis is the analysis of the changes in the proportions of selected benchmarks includes total revenues, total assets, total liabilities and so on. We use it to analyze the profitability by using the common size income statement and in financing and investment by using the common size balance sheet. The formula is:

$$Proportion = \frac{\text{an item of this bench}}{\text{benchmark}} \cdot 100\% \quad (2.4)$$

Through this formula, we can analysis the degree of the importance of each item in operation of the company. The analyst can use the information to compare these proportions and find the trend across time and the company's industry. *The larger the proportion of the item is, the higher degree of importance, the bigger effect on benchmark.*<sup>3</sup> This method is really a useful way to compare the different periods in statement and in time.

### 2.2.2 Trend analysis

Trend analysis is a kind of analysis that people can try to predict the future movement of a company based on its financial data. It is also known as comparative analysis. Analysts use the past data and make a prediction about what will happen in the future of a company, they will

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<sup>3</sup> Robinson, Thomas R. et al. *International Financial Statement Analysis*. 2nd edition. New York: John Wiley and Sons, 2012. ISBN: 978-0-470-91662-9

describe their growth changes in the direction of using trend analysis to show its financial position, examine its operations and the trend of cash flow. It can be a powerful tool to develop and open minds by exploring and comparing the developments. Generally the financial statement's information has already been prepared to compare. It's simple and helpful because we only use the data and make a graph to see its movement, investors can make decision quickly.

For investors, to identify the trend in a company and evaluate its financial situation and the results of its current operating condition is necessary, so it is very important to determine the main cause of changes in a company's financial situation and operating condition, so based on the information, they can describe and predict the trends of the future financial development of a company. We call this method as the form of dynamic analysis, *it is the testing and evaluation of a program by executing data in real-time*. There is approach called dynamic analysis statistically, it is the financial report with the same indicator during different periods and we can compare directly to the ratio and find their trends and predict its future development.

There are two kinds of dynamic ratios include fixed base dynamic ratio and chain dynamics ratio. The first ratio is the value of the comparative analysis, it has fixed base index value. The second ratio is based on primary analysis of the value and its based period value is calculated by the dynamic ratio.

In order to compare the changes, we need to find appropriate method to evaluate the company's financial position and operating condition, it will be better to calculate both the absolute values of the indicators changes, using this method can avoid the one-sided results. In this method, we calculate the percentage of each component of all the data for each item to describe the trends which in connection with the financial activities. This method is easier to operate, it can be used in the same financial situation of a company during different period also can be useful for different companies. But when the situation is more complicated, the method of calculation will be more complicated.

By using this method we can find the factor that changes most in trend analysis, then we can specifically analysis this factor and find the reason. By this method, we can identify and predict the financial trends in a company and judge its financial condition whether it's good for investors.

There are 4 steps to analysis the business performance for trends:

1. making financial calculations,
2. observing the ratios,
3. creating tables from the information,
4. making graphs and find the trend over the time.

Trend analysis is a useful method because we can combine with other financial methods to make financial observations, it's a really power tool to make a business decision. So by using this method we can make a historical data and make prediction then a company can improve their business.

### **2.2.3 Financial Ratio Analysis**

Financial ratio analysis is in the form of financial ratios to assess the financial health of the company by comparing the financial data. It is the useful way to assess the performance whether is better or worse for companies' financial position.

Financial ratio includes five groups: Profitability ratios, liquidity ratios, solvency ratios, asset management ratios and market ratios.

#### **Profitability ratios**

Profitability refers to the ability that the company can generate profits from invested capital in the form of return during a period. Generally, the higher the profitability ratios are, the better competitive position of the company. It can measure whether resources are used effectively, whether the financing activities are reasonable, whether returns can come up to expectation. Profitability ratios are the very important indicator, because profit is the main target for every company, it can affect the future financing behavior of the company.

There are some main ways to measure the profitability like *OPM* (operating profit margin), *NPM* (net profit margin), *ROE* (return on equity), *ROA* (return on assets).

$$OPM = \frac{EBIT}{Rev} \text{ or } \frac{OP}{Rev} \quad (2.5)$$

where *OPM* is the abbreviation of operating profit margin, *Rev* is revenue, *EBIT* is earning before interest and tax, *OP* is operating cost. This ratio shows that how well that the company manages its operation and how well the revenues are being generated and operating costs are being controlled. It also measures that operating profit per one unit of the revenues and a company's pricing strategy and operating efficiency. If the operating margin is healthy, the company is required to be able to pay for its fixed costs. Generally, the higher the operating profit margin is, the better the profitability is.

$$NPM = \frac{EAT}{Rev} \quad (2.6)$$

where *NPM* is the abbreviation of net profit margin, *EAT* is earning after tax. It measures net income (as a percentage) per one unit of revenues or net profits divided by sales. It measures that how much that sales of a company can actually keep in earnings. It is a very useful ratio when comparing the companies in the same industries. Generally, the higher the net profit margin is, it indicates that a better profitable company is, it can have better control over its costs compared with the competitors.

$$ROA = \frac{EAT}{A} \text{ or } \frac{EBIT}{A} \quad (2.7)$$

where *ROA* is the abbreviation of return on assets, *EAT* is earning after tax, *EBIT* is earning before interest and tax. This ratio measures net profit or operating profit as a percentage for each unit of company's assets. The higher ratio indicates the better use of assets in a company.

$$ROE = \frac{EAT}{Equity} \quad (2.8)$$

where *ROE* is the abbreviation of return on owner's equity, *EAT* is earning after tax, it is the amount of net income returned as a percentage of owner's equity, it measures the company's efficiency at generating profits from every unit of owner's equity, it's the main ratio to measure the shareholder's value, and it can represent the ability of a company to raise money in market. The higher the ratio is, the better use of equity in a company.

## **Liquidity ratio**

Liquidity ratio reflects the company's ability to meet its immediate or short-term liabilities and obligations. The liquid assets are usually in form of cash or can be quickly converted into cash. Generally the liquidity of company shows its ability to get cash available when needed to meet its short-term obligation.

There are three main ways to measure its liquidity:

### **Current ratio**

In formula (2.9), it measures the amount of current assets to its current liabilities and shows ability to repay its debts over the period of time. It is widely used of measuring the liquidity of a business and its ability to pay back the debt. The lower the current ratio is, the better liquidity is. It is calculated in the following formula:

$$\text{Current Ratio} = \frac{\text{Current assets}}{\text{Current Liabilities}} \quad (2.9)$$

### **Quick ratio**

In formula (2.10), it is the stricter test of company's liability, the current assets are adjusted for inventories, and it's generally less liquid. It measures the ability of a company to pay its debts by using cash. The lower the quick ratio is, the better liquidity is. It is calculated in the following formula:

$$\text{QuickRatio} = \frac{\text{Current assets} - \text{inventories}}{\text{Current liabilities}} \quad \text{Or} = \frac{\text{Cash} + \text{account receivable}}{\text{Current liabilities}} \quad (2.10)$$

### **Cash ratio**

In formula (2.11), it shows the assets that are in the form of cash and represents the marketable securities can be sold immediately in the market within a few hours or days. It measures the ability of company to repay its current liabilities only by using cash equivalents. The lower the cash ratio is, the better liquidity is. It is calculated in the following formula:

$$\text{Cash Ratio} = \frac{\text{Cash} + \text{Marketable securities}}{\text{Current Liabiliteis}} \quad (2.11)$$

## **Solvency Ratios**

These ratios measure company's ability to meet its long-term obligations. It can also be called financial leverage ratios, they measure how the company is financed. Generally, the lower solvency ratio of a company, the bigger possibility that it may default on its debt obligations.

There are four main ways to measure its solvency:

### **Debt ratio**

In formula (2.12), it shows what percentage of the company's asset is financed by liabilities. It is a simply debt ratio and it measures the ratio of total debt of a business activity to its total assets. The higher the ratio is, the more leveraged of a company and the greater of its financial risk. Debt ratios vary widely in the industries. It is calculated in the following formula:

$$\text{Debt ratio} = \frac{\text{total debt (total liabilities)}}{\text{Assets}} \quad (2.12)$$

### **Debt-to-capital ratio**

In formula (2.13), it measures the amount of company's debt relative to company's capital. Higher debt with the capital means higher risk of insolvency. The total debt includes short-term debt and long-term debt, the short-term debt is in short maturity, usually one year or less, so if a company has more short-term debt than available cash to cover its debt payment, then the company will be forced to face and take responsibility for its debt, it means that the company is in poor financial health. Long-term debt usually means that the loan with maturity longer than one year, the borrowers need to pay the interest payment for the debt. The ratio is calculated in the following formula:

$$\text{Debt-to-capital ratio} = \frac{\text{Total debt}}{(\text{shareholder's equity} + \text{debt})} \quad (2.13)$$

### **Debt-to-equity ratio**

In formula (2.14), it's similar to debt ratio, it relates the amount that that company's debt relative to company's equity. We only need to evaluate the relationship between the debt and equity. If the ratio is higher than one, the company needs to use more debt for assets financing than equity. It is calculated in the following formula:

$$\text{Debt-to-equity ratio} = \frac{\text{total debt}}{\text{equity}} \quad (2.14)$$

### **Interest Coverage**

In formula (2.15), it shows the company's operating profit is able to meet current interest payments. It's the ratio of earnings before interest and tax (*EBIT*) of a company to its interest expense during a given period, it is used to determine how well a company can pay interest on outstanding debt. Generally, the lower the ratio is, the more the company is burdened by its debt expenses. It is calculated in the following formula:

$$\text{Interest Coverage Ratio} = \frac{\text{EBIT}}{\text{annual interest expense}} \quad (2.15)$$

### **Asset management (activity) ratios**

They measure how well a company uses its assets, it also can be called assets utilization, and it has a direct impact on liquidity. This ratio indicates that how much a company invested in a particular assets relative to the revenues that the assets are generating. It is important to show that how well the company's management and the ability to generate money

There are four ways to measure its activity:

- average collection period,
- inventory turnover,
- receivable turnover,
- total asset turnover.

### **Average collection period (ACP)**

In formula (2.16), *ACP* measures the conversion of accounts receivable into cash, it indicates the days that a company need to collect the receivables from the customers and clients. The credit sale is the total amount net credit sales during period. The relationship of *ACP* is in the following:

$$\text{ACP} = \frac{\text{accounts receivable}}{\text{credit sales}} \quad (2.16)$$



**Inventory turnover (*IT*)**

In formula (2.17), it's the key operation for many entities. It measures the number of times inventory is sold or used during a period such a year. It is the core operations, it the resources in inventory and it can indicate the management effectiveness of a company. We can use the days in period which can be divided by the inventory turnover formula then calculate the days that takes to sell the inventory, it named *DOH*. The relationship of *IT* is in following:

$$\text{Inventory Turnover} = \frac{\text{Cost of goods sold}}{\text{average inventory}} \quad (2.17)$$

**Receivable turnover (*RT*)**

In formula (2.18), it measures the efficiency of a company to collect its credit sales. In general, a high value of *RT* is popular within investors, if the figure is lower, that means its inefficiency in collecting sales of a company. So increasing the accounts receivable during a period usually indicates the improvement of the ability of collecting the cash on the revenues. We can use the days in period which can be divided by the receivable turnover formula then calculate the days that takes to sell the inventory, it named *DSO*. The relationship of *RT* is in following:

$$\text{Receivable Turnover} = \frac{\text{Revenues}}{\text{Receivables}} \quad (2.18)$$

**Total asset turnover (*TAT*)**

In formula (2.19), it's an efficiency ratio that shows how successfully the company is using its assets to generate revenue. It indicates how well a company is using its asset to generate revenue. Generally, the higher the ratio, the better the situation is. This ratio is a key component of DuPont analysis, we will introduce in the next method. The relationship of *TAT* is in following:

$$\text{Total Assets Turnover} = \frac{\text{Revenues}}{\text{asset}} \quad (2.19)$$

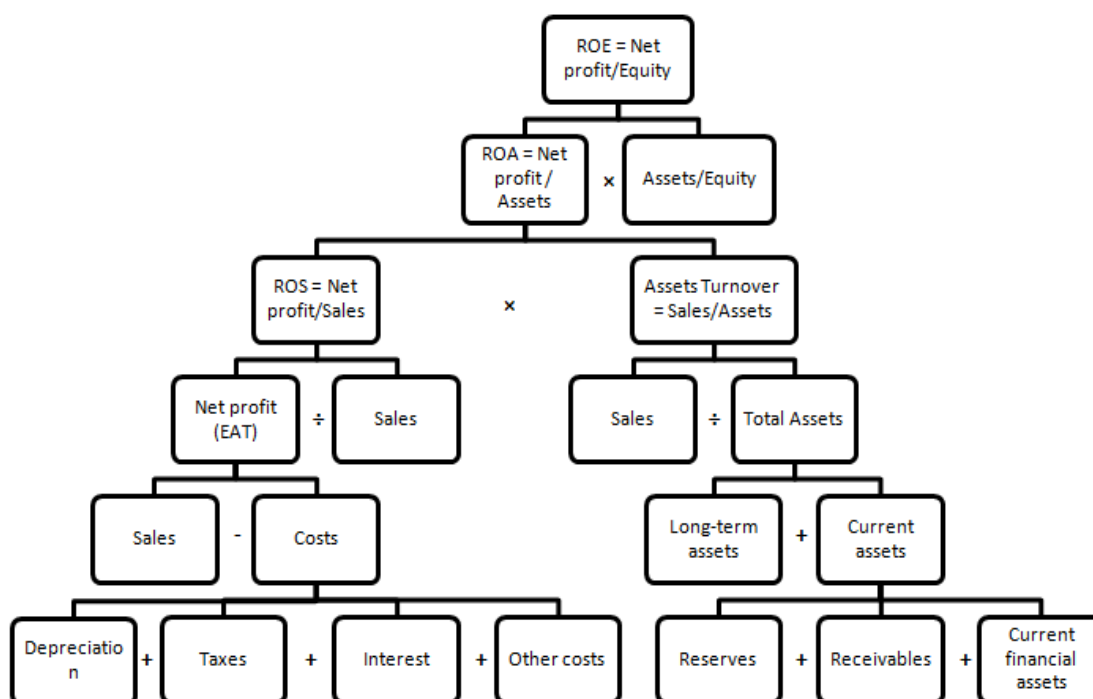
**2.2.4 Pyramidal Decompositions**

Pyramidal decompositions can analyze what drives the value of financial ratios, for example, which factors have impact on its value or evolution. The principle of it is to express selected

ratio as a product of component ratios. The aim of it is to find out which component has the most contribution of the financial ratio.

We can simply know about pyramidal decomposition structure by the following table:  
(here we use the example about *ROE*)

**Table 2.4 Pyramidal Decomposition on *ROE***



Source: <https://managementmania.com/en/duPont-analysis>

This method is used for measuring the efficiency of the basic factors. It completes the method of financial ratios.

The fundamental example of the pyramidal decomposition is the DuPont analysis. For example, in formula (2.21), the decompose *ROE* ratio has three component ratios including net profit margin, the assets turnover and the leverage.

$$ROE = \frac{\text{net profit}}{\text{equity}} = \left( \frac{\text{Net income}}{\text{Revenues}} \right) \cdot \left( \frac{\text{Revenues}}{\text{Total assets}} \right) \cdot \left( \frac{\text{Total assets}}{\text{equity}} \right) \quad (2.23)$$

If we want to separate the effects on interest and taxes, we can decompose the net profit margin as following:

$$\frac{\text{Net income}}{\text{Revenues}} = \frac{\text{Net income}}{\text{EBT}} \cdot \frac{\text{EBT}}{\text{EBIT}} \cdot \frac{\text{EBIT}}{\text{Revenues}} \quad (2.24)$$

So we know from the formula (2.24) that it has three components include tax burden, interest burden and operating profit margin. *EBT* is the abbreviation of earning before tax, *EBIT* is the earning before interest and tax.

After substitution into DuPont analysis we can get that:

$$ROE = \frac{\text{Net income}}{\text{EBT}} \cdot \frac{\text{EBT}}{\text{EBIT}} \cdot \frac{\text{EBIT}}{\text{Revenues}} \cdot \frac{\text{Revenues}}{\text{Total assets}} \cdot \frac{\text{Total assets}}{\text{Equity}} \quad (2.25)$$

We can see from this formula that it has five components include tax burden, interest burden, *EBIT* margin, asset turnover and financial leverage. *EBT* is the abbreviation of earning before tax, *EBIT* is the earning before interest and tax.

The influence quantification can analyze indicators whose change have caused change in the basic ratio and quantify which component ratios contributed to the change in basic ratio at most.

There are four methods for quantification of influence.

#### **a) Methods of gradual changes.**

It can quantify the change in the basic ratio caused by the change in the component ratio.

The decomposition with 3 component ratios are as follows:

$$\begin{aligned}
\Delta x_{a1} &= \Delta a_1 \cdot a_{2,0} \cdot a_{3,0} \cdot \dots \cdot a_{n,0} \\
\Delta x_{a2} &= a_{1,1} \cdot \Delta a_2 \cdot a_{3,0} \cdot \dots \cdot a_{n,0} \\
\Delta x_{a3} &= a_{1,1} \cdot a_{2,1} \cdot \Delta a_3 \cdot \dots \cdot a_{n,0} \\
\Delta x_{an} &= a_{1,1} \cdot a_{2,2} \cdot a_{3,0} \cdot \dots \cdot \Delta a_n \\
\Delta x_{ai} &= \Delta a_1 \cdot \prod_{j>i} a_{j,0} \cdot \prod_{j<i} a_{j,1}
\end{aligned} \tag{2.26}$$

In this formula,  $x$  is the basic ratio,  $\Delta x$  is the absolute change of the basic ratio,  $a$  is the component ratio, and  $\Delta a$  is the absolute change in the component ratio.  $\Delta x_{ai}$  is the absolute change in the basic ratio cause by the change in the first (a) component ratio.

#### b) Logarithmic decomposition method.

Using this method, we only need just one formula for the impact qualification regardless of how many component ratios we have. We can rank the component ratios by degree of influence, the company's manager can get advices from the rank.

The impact of the  $i$ -th component ratio on the change in the basic ratio is calculated as following:

$$\Delta x_{a_i} = \frac{\ln I_a}{\ln I_x} \cdot \Delta y_x \tag{2.27}$$

In this formula,  $x$  is the basic ratio,  $\Delta x$  is the absolute change in the basic ratio,  $I_x$  is the index of change in basic ratio,  $I_a$  is the index of change in component ratio.

#### c) Functional decomposition method

This method works with the relative changes in basic and component ratios.

$$\begin{aligned}
\Delta x \text{ (relative)} &= R_x = x_1 - x_0, \\
\Delta a_i \text{ (relative)} &= R_{ai} = \frac{(a_1 - a_0)}{a_0}
\end{aligned} \tag{2.28}$$

The influence of the component ratio on the basic ratio:

$$\Delta x_{a1} = 1/R_x \cdot R_{a1} \cdot (1 + 1/2 \cdot R_{a2} + 1/2 \cdot R_{a3} + 1/3 \cdot R_{a2} \cdot R_{a3}) \cdot \Delta x$$

$$\Delta x_{a2} = 1/R_x \cdot R_{a2} \cdot (1 + 1/2 \cdot R_{a1} + 1/2 \cdot R_{a3} + 1/3 \cdot R_{a1} \cdot R_{a3}) \cdot \Delta x \quad (2.29)$$

$$\Delta x_{a3} = 1/R_x \cdot R_{a3} \cdot (1 + 1/2 \cdot R_{a1} + 1/2 \cdot R_{a2} + 1/3 \cdot R_{a1} \cdot R_{a2}) \cdot \Delta x$$

We can find an example to calculate the results using these three methods and compare them. We will see that the results are similar, the difference between these methods are small. But these three methods are all very important in calculating influence qualifications. We can use the pyramidal decompositions to analysis the ranks in financial ratios and predict them.

### **3. Profile of IKEA Company**

IKEA was founded in Sweden, it is a worldwide furnishing company for selling Scandinavian-style furniture and other home-based goods. It is one of the most famous international companies in the world. In this chapter, we will introduce some basic information and more details about IKEA including three parts.

#### **3.1 Basic information of the company**

IKEA was founded by Ingvar Kamprad in 1943, it has become the world's largest furniture retailer since 2008. "Create a better daily life for most people" is the direction of IKEA since its inception has been working. IKEA brand has always been devoted to improving the quality of life and create products that most customers can afford, have good full-featured design and low-cost household items are their business purpose. IKEA also has put much effort to create business to approach to the interests of customers and the community center, it committed to undertake the environmental protection and social responsibility, and so it has a good reputation within customers.

IKEA company's products have many series including seat/sofa series, office supplies, bedroom series, kitchen series, lighting, textiles, cooking utensils, house storage series, children's products series which have about 10,000 products. Customers can freely choose kinds of goods they want to buy, IKEA is a company that attaches much importance to many small details, and so it can create many new convenient things for customers. Nowadays, IKEA open its own restaurant for customers so they can enjoy low price and high quality's food.

#### **3.2 The history of the company**

IKEA has a long history since 1943. As a worldwide company, *IKEA has many branches including in Europe, Asia, North America, Oceania, and Africa. From September 2014, Ikea owns and operates 351 stores in 43 countries with over 13900 employees.*

In 1943, IKEA was founded by Ingvar Kamprad who is a native of Sweden. He received a gift from his father for doing well in school then he formed IKEA. *The company initially sold basic*

*items like pens, wallets, picture frames, table runners, jewelry, nylons stockings and watches at a low price.*

In 1948, IKEA began to produce range of products about furniture and decide to increase the size of its product lines. At this time, the furniture retailer developed the initial shape. In order to win the price war with their main competitor, IKEA opened a showroom in Sweden to attract the customers, because they can make a decision whether it's worth to buy. In old opinion, customers can only view furniture through catalogue, but in IKEA, customers were allowed to access to view and touch the furniture, also IKEA decide to design its own furniture, the "flat-packs and self-assembly" concepts allow employee can disassembled a table to prevent damage during the transport, so IKEA company has created a competitive advantage. For IKEA, this process is very meaningful and a successful exploration.

In 1963, IKEA was looking for expanding its future markets through franchising, also in this time, the new furniture concepts were born in company. *To ensure continuation and long-term independence of IKEA, the founder created a new ownership structure and organization.* The foundation has the major portion of IKEA, meanwhile, the IKEA group of companies have the right to franchise the worldwide IKEA concept.

In 1990, IKEA began to design furniture that aimed at specified customer group like children. Also the official website was launched to provide various information to customers. Nowadays IKEA can provide services for many occasions like home, education, small business owners, and newly-wed couples. During this period, IKEA attached more and more importance to the sustainability projects.

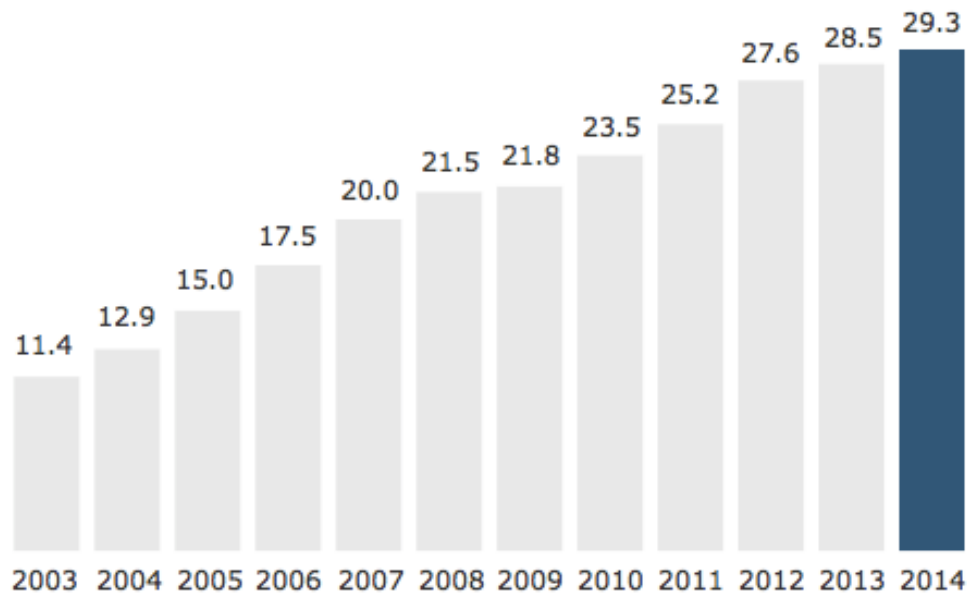
In 2014, IKEA has total sales EUR 28.7 billion, 315 stores in 27 countries and mainly in Europe, its products has about 9500 in the range with 147000 co-workers, there are 1002 home furnishing suppliers in 51 countries. The shop visits can have 716 million and web visits have more than 1.5 billion. Its catalogues printed 217 million in 30 languages. Also its food has EUR 1.46 billion yearly turnovers.

Currently, customers can shop online now in IKEA page. *Other innovations include the boards with patterns created on them directly, it called "print on board", also a concept known as*

*“product recovery concept”, it means that returned products are repaired instead of being thrown away where possible.*

We can see the total revenue in IKEA from the following chart

**Chart.3.1 Total revenue of IKEA in billions of euros 2003-2014**



Sources: [http://www.ikea.com/ms/en\\_GB/about-the-ikea-group/company-information/index.html](http://www.ikea.com/ms/en_GB/about-the-ikea-group/company-information/index.html)

We can see from this graph that the total revenue in IKEA is increasing from 2003 to 2014, is shows a good financial condition from its change of historical data.

### **3.3 The business strategy of the company**

IKEA's success lies in its unique ways of research and business model.

#### **3.3.1 Unique operation structure- Stichting INGKA Foundation**

IKEA has its unique way of organization structure- Stichting INGKA Foundation. *Its purpose is to fund charity through the Stichting IKEA Foundation in the Netherlands and to reinvest in the IKEA Group.* IKEA Group (INGKA Holding BV and all its controlled entities) has a long-term vision to ensure the independence and ownership structure and it is for long-term. There

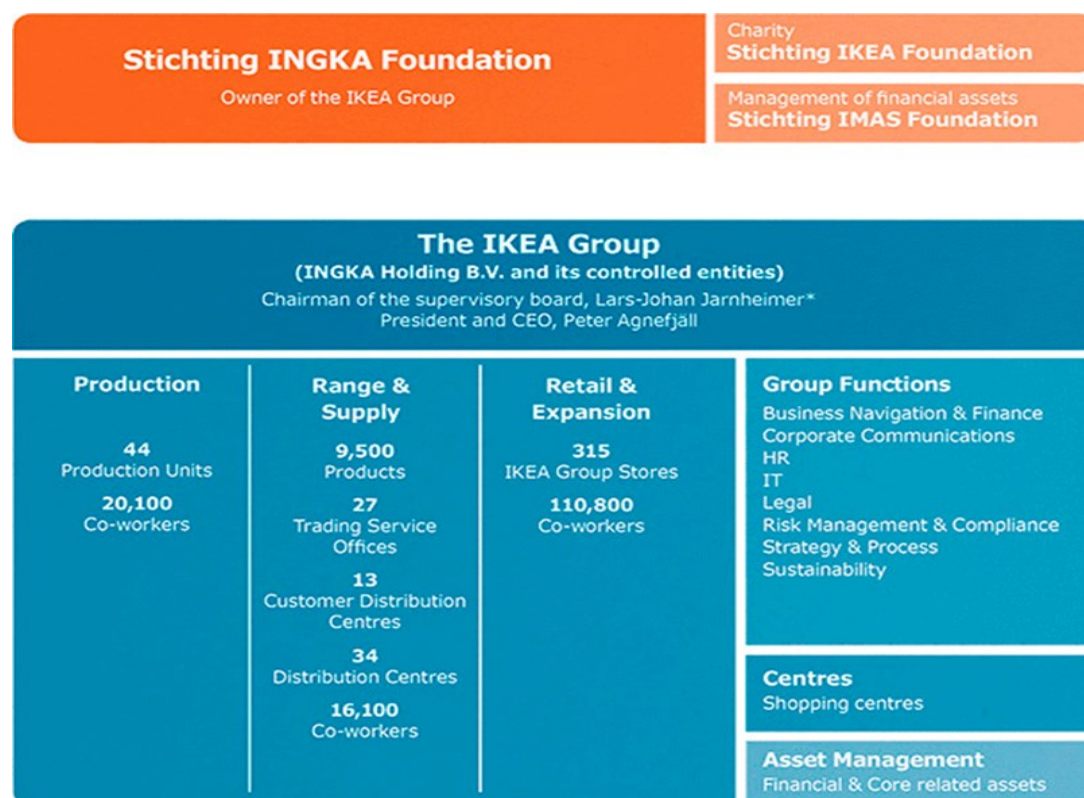


are only two ways that its fund can be used: *reinvested in the IKEA group or donated for charitable purposes through the Stichting IKEA Foundation.*

Ingvar Kamprad, the Senior Advisor & Founder of IKEA said that “*I decided that the stock market was not an option for IKEA. I knew that only a long-term perspective could secure our growth plans and I didn’t want IKEA to be dependent on financial institutions.*” We can find the reason from the founder of IKEA and understand its unique way of business management and how to operate well such a big company and keep it independent.

We can simply see from the chart 3.2 that IKEA Group is responsible for operating the entire value chain, including from product line strategy, product development, production, distribution, and retail, so then it can facilitate the coordination of funds between different countries and reasonable turnover tax. The group is managed by CEO and president, Peter Agnefjäll. Now in total, we can find its operation in 42 countries in the world.

**Chart 3.2 Stichting INGKA Foundation<sup>4</sup>**



Source : [www.ikea.com/ms/en\\_GB/about-the-ikea-group/company-information/index.html](http://www.ikea.com/ms/en_GB/about-the-ikea-group/company-information/index.html)

\* From January 2015, Göran Grosskopf as a new chairman of the IKEA Group

<sup>4</sup> [http://www.ikea.com/ms/en\\_GB/about-the-ikea-group/company-information/index.html](http://www.ikea.com/ms/en_GB/about-the-ikea-group/company-information/index.html)

The headquarters of IKEA is in Leiden, Netherlands. And in the Netherlands, *Inter IKEA Systems B.V. is the owner of IKEA Concept and as the worldwide IKEA franchisor, The IKEA Group franchises the IEKA retail system from it.*

### **3.3.2 Research and innovation**

It has four parts including market design and positioning, low-cost design, pattern design and sustainable strategy.

**Market design and positioning.** IKEA will interview 6000 people every three year and make a comprehensive market research. At the same time, IKEA has a special department to oversee and expects which series will be welcomed in 5 years. They have its own independent department to design, it has unusual design of products, and they are always seeking for the unique style with simple, nature, pure and fresh with the best quality of design. So IKEA make a good balance between marketing and designing. A wide range of products make IKEA become more popular within customers, there are more than 10000 kinds of products for customers to choose, basically, all kinds of customers can find their perfect furnishing products in IKEA because of its wide functions and styles.

Their operation principle is to provide a wide range of, beautiful and useful, also affordable furnishing products for common people to buy , it is their market positioning. In European and American countries, their aim is to sell the products for common people and because of its excellent quality and reasonable price, new style and nice services, it is very popular in these area. After expanding its market in China, the situation is changed, though there is a big potential market in China, but the common level of consume is relatively low, the low price market is nearly to be saturated and the competition is very fierce, so they focus on the relatively rich rank in the big city, so their market positioning in China is for those white collar who want to buy top products but cannot afford the high price, this positioning is very clever and exact, so this thought is very successful in Chinese market.

In 1997, IKEA exquisitely find the kids' furnishing market, it has a big potential and the competition in this field is not too fierce. In order to expand this market, IKEA put specialized effort on it and make exhibition halls for kids and it supply foods, so kids all like it and indirectly urge people to go shopping in IKEA, it made a right marketing decision.

**Low-cost design.** IKEA has strong cost consciousness. As we know that their business idea is *“to offer a wide range of well-designed, functional home furnishing products at price so low that as many people as possible will be able to afford them”*. So frugal, simple, cheap and convenient is the common view of IKEA founder. IKEA is very good at reducing costs from each chain of the production process, it also has specific regulation about how to use the electricity to reduce the cost of using electricity. Some shops also provide the service of furniture recycling for reuse treatment. IKEA not only has awareness of frugality, it also enables people to make a big progress on the product design, like tablet design, self-assembly furniture concept and flat packages, they remind people of cost consciousness and they do decrease the costs and fees.

In IKEA, they have a model to lower the price, usually they will confirm the price firstly then think about designing the products, during the process of designing the products, IKEA attach much importance to the teamwork, so the designers, product developers, purchasing staffs can connect with each other closely and produce a perfect product. In order to lower the price, IKEA will try to think to reach every aspect of matter, it can be related with the colors, sizes and transportation.

IKEA always innovate to lower the price, they find the new materials and technology to increase the quality of a product and lower its price. The worldwide producing management and logistics system also good for lowering the costs, IEKA use the flat package to lower the transportation costs. Also there is one important point is that IKEA make corporation with the customers to lower the costs, customers can use the catalog of IKEA and find the products and assemble by themselves, for the customers, they can enjoy the low price, for IKEA, they can lower their costs and keep their advantage about its low price.

**Experience-oriented marketing.** It has five parts including participation links, experience links, design links, individuation links and transportation links. In the shops, staffs will provide customers with something like pens, rulers and papers, then the customers can join the process of designing personal home furnishing. In every shops of IKEA, customers can touch and feel the furniture and make their own decisions. In IKEA, customers can use kinds of components to design their own fond furniture. IKEA use its limited products to create more combinations. Because of the standardized modular flat building, it allows customers to use a whole package

to make transportation more convenient. It successfully made IKEA become a symbol of a kind of life style.

IKEA also use the exhibition of catalog as one of most important part of their marketing strategies. From 1951, IKEA issued their products catalogs and sent for customer freely every year. From the catalogs, customers can see the pictures and price of the products, because of the careful design of the designers, customers also can feel its functional and image of the IKEA's products and find the practical solutions and inspiration of furnishing layout. The value of catalogs of IKEA is not only for advertising, for customers, it's a decorated guidance. For IKEA, they do not only sell the furnishes, the more important for them is to sell kinds of lifestyle, a natural attitude towards life. IKEA sell their lifestyle all over the world, and the catalog is one of the important part, for customers, buying the product is the best way to achieve this kind of lifestyle.

**Sustainable strategy.** It is one of the important parts of IKEA's business strategies. This strategy can be seemed as an investment for the future, it is their main financial principle of its group, it is a long-term investment. IKEA want to make itself accessible, so that more people can create a better daily life, so IKEA will reinvest part of their profits for their new stores, development of their products and find sustainable solutions and constantly find ways to lower the price for customers. Nowadays it seems more and more important. They are always searching for a sustainable future as their old tradition, because they want to create a better life for every people and have a positive influence on our unique planet, so IKEA has a very good social image to the customers, IKEA proved the necessity of it. For many years, IKEA always focused on optimizing resources and making progress. IKEA made annual sustainability report and summary to make progress step by step. Today, more and more raw materials like cotton come from sustainable sources and it is trying to use efficient and environmental energy in IKEA Company, it aims at benefitting on the people and planet to create a better future.

**Globalization strategy.** As the biggest furnishing production and retailing company in the world, it is very necessary for IKEA to expand its market. Globalization has two parts include globalization of product and globalization of market. In the 1950's, IKEA was forced by the domestic partners, so IKEA had to find new materials suppliers oversea, then they found the cost was lower, now it already become a worldwide purchasing company, it has 1300 material suppliers in the 53 countries, it can be helpful for designers to find the most appropriate one to

produce their products. In the early of 1970's, the furnishing market didn't have much space to develop in Sweden, so IKEA began to think about expanding its furnishing market in the world, from 1974's to 2014's, IKEA had become a company that own stores from 10 to 351 in 46 countries, they had revenue about 28.506 billion in 2013, but there are only 8% selling from Sweden, surely it is a worldwide company. Nowadays, IKEA still find new business chances in the world.

## **4. Financial Analysis of the IKEA Company**

In this chapter, we will analyze the financial condition of IKEA Company. Firstly we use the common size analysis method including horizontal analysis and vertical analysis to compare the changes according to the information of each financial statement during 2010 to 2013; then we use the trend analysis to describe the changes and spot the trend of a company's financial activity during four years; after we will use the financial ratio analysis method to analyze the 4 types of the basic ratio of the company. The 4 types basic ratios including profitability ratios, liquidity ratios, solvency ratios, activity ratios, we will discuss the connection between these. Financial ratios analysis is one of the most essential methods of financial analysis, we can use the data to compare the financial ratio and evaluate the financial health of a company. Lastly we will use the pyramidal decomposition method to analyze the ROE, explain its components to compare and find out the biggest influence factor on ROE in different year.

The source of information for calculation is from the Annual Report of IKEA Company. From the IKEA annual financial report we can know firstly that the main financial principles in IKEA group are to ensure its financial stability, independence and flexibility, they earn the money before they spend it. We can make this conclusion in the following financial analysis of IKEA.

### **4.1 Common-size Analysis**

In this chapter, there are two main financial statements are analyzed and described by using the common-size analysis.

#### **4.1.1 Common-sized analysis of Balance sheet**

This part is the financial situation of Ikea Company from the balance sheet. In this part, we describe the main data in the balance sheet and analyze the reason of causing it. The balance sheet will be divided into two parts including assets, liabilities and equities.

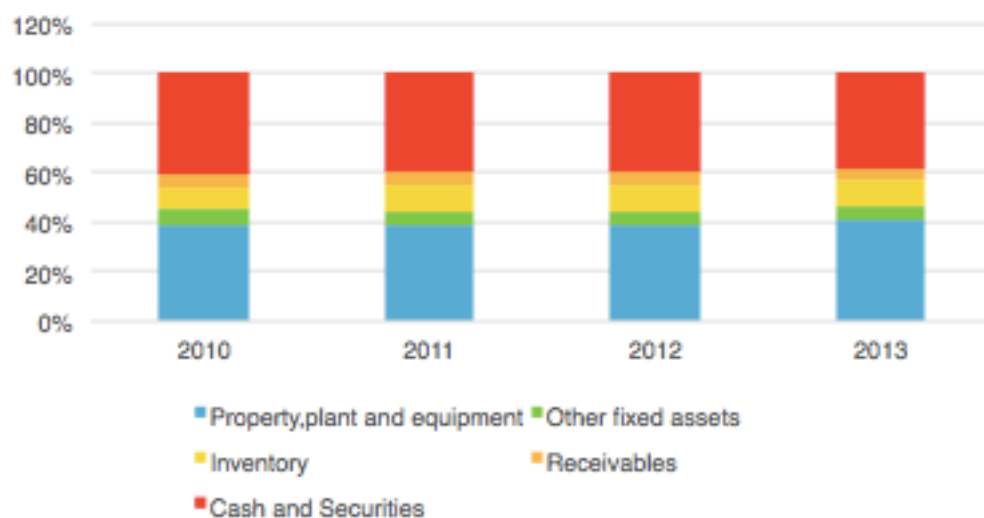
**Table 4.1 Common-size analysis of asset**

(IN MILLION OF EURO)	2010	2011	2012	2013
Property, plant and equipment	39%	39%	39%	41%
Other fixed asset	7%	6%	6%	6%
Inventory	8%	10%	10%	10%
Receivables	5%	5%	5%	5%
Cash and Securities	41%	40%	40%	38%
<b>Total assets</b>	100%	100%	100%	100%
<b>Total fixed assets</b>	45%	44%	45%	47%
<b>Total current assets</b>	55%	56%	55%	53%

Source: Own Calculation

The percentage of these data was calculated is an item of the benchmark divided by the benchmark during a specific period, we calculate via the formula (2.4), so we use the original data to calculate and find the percentage in different parts. We can add up all the percentage in the same year and the result is 1.

So we make the following chart 4.1 based on the percentage data in the table 4.1, we can find the changes of different parts during this period.

**Chart 4.1 Common-size analysis of asset**

Source: Own calculation

We can see from the table and chart, during 2010 to 2013, the total fixed assets is increasing, the most increased period is 2012-2013, about 2%, so relatively, the total current assets is decreasing during this period. During the 2010 to 2013, Ikea Company has bought more property, plant and equipment, then the proportion of cash and securities decrease. So the trend of total fixed assets is increasing, the total current asset is decreasing. Compared to the property, plant and equipment with cash and securities part, we can find that from 2010-2012, the most biggest percentage part in the five parts is the cash and securities, but in 2013, we see that property, plant and equipment part replaced the cash and securities, the distinguish between these two parts is reducing, it stated that IKEA was increasing the proportion of the part of property, plant and equipment and relatively decreasing the cash and securities part. Seen from the whole table, we find the proportion of inventory is increasing too, we can make a conclusion that IKEA was increasing their proportion of fixed assets and it is continuous, the reason is that the growth of new investments and expansion of the new IKEA stores, warehouses, retails centers and factories. In the annual report of 2013, we find that IKEA invested 1.9 billion euro in new stores, factories, renewable energy and shopping centers, they were investing in sustainable growth, so IKEA use assets to develop their core business. And also the cash and securities always are a big part in the balance sheet because the company needs to finance most of this with the expansion with their own money. Next we talk about the liability and equity in the following table and chart:

**Table 4.2 Common-size analyses of liability and equity**

(IN MILLION OF EURO)	2010	2011	2012	2013
Group equity	55%	62%	70%	71%
Long-term liabilities	10%	8%	6%	5%
Other non-current liabilities	3%	4%	4%	4%
Short-term liabilities	14%	11%	10%	8%
Other payables	19%	17%	17%	12%
<b>Total equity and liabilities</b>	100%	100%	100%	100%
Group equity	55%	61%	65%	70%
Total non-current liabilities	14%	11%	9%	8%
Total current liabilities	31%	28%	26%	22%
<b>Total equity and liabilities</b>	100%	100%	100%	100%

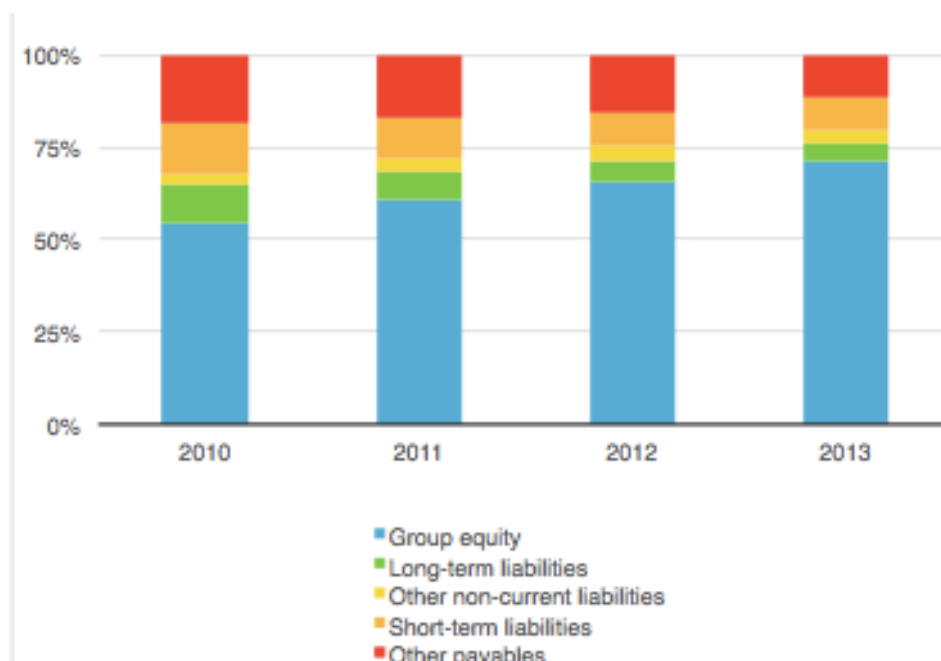
*Source: Own calculation*



We use the same method as we said in the balance sheet for assets, we calculate via the formula (2.4), now we use the data for the liabilities and equities, so we can find the proportion in different parts, all the sum is 1 in the same year.

So we use the calculation results to make the following chart 4.2 to find the changes in different year during 2010-2013.

**Chart 4.2 Common-size analyses of liability and equity**



*Source: Own Calculation*

We can see from this table and chart that the group equity is increasing during 2010 to 2013, nearly 15%, the most increased period is from 2010 to 2011. And the total non-current liabilities and total current liabilities is decreasing in this period, nearly 6% and 9%, the most decreased period is from 2010 to 2011 and 2012 to 2013. It shows the group equity of Ikea is becoming stronger and stronger than before, the proportion of liabilities is decreasing. Whatever the total current or long-current liabilities, the proportion was always decreasing, during these four years, no matter seen from the lengthways or crosswise, the proportion of group entity is increasing and the most biggest part in all the activities and the percentage is over 50%. Compared with the total current and non-current liabilities, the proportion of total current liability is bigger than total non-current liability, it stated that more liability is in current and would be pay back soon later, it indicates a good financial condition in IKEA, there was no

debt problem in it, and the percentage of group equity is big, because of its unique business management-structure. IKEA foundation, this group structure can ensure its ownership organization and keep the independent, this foundation provides a long term approach to fund charity from it, so its group equity can keep increased during this period. We can see that IKEA keep a good balance between entity and liability, it has strong ability to face the kinds of financial situations and deal with it well.

#### 4.1.2 Common-sized analysis of Income Statement

This part is the financial situation of Ikea Company from the income statement. We can see the total revenue and the relative factors' change during 2010 to 2013.

**Table 4.3 Common-Size Analysis of Income Statement**

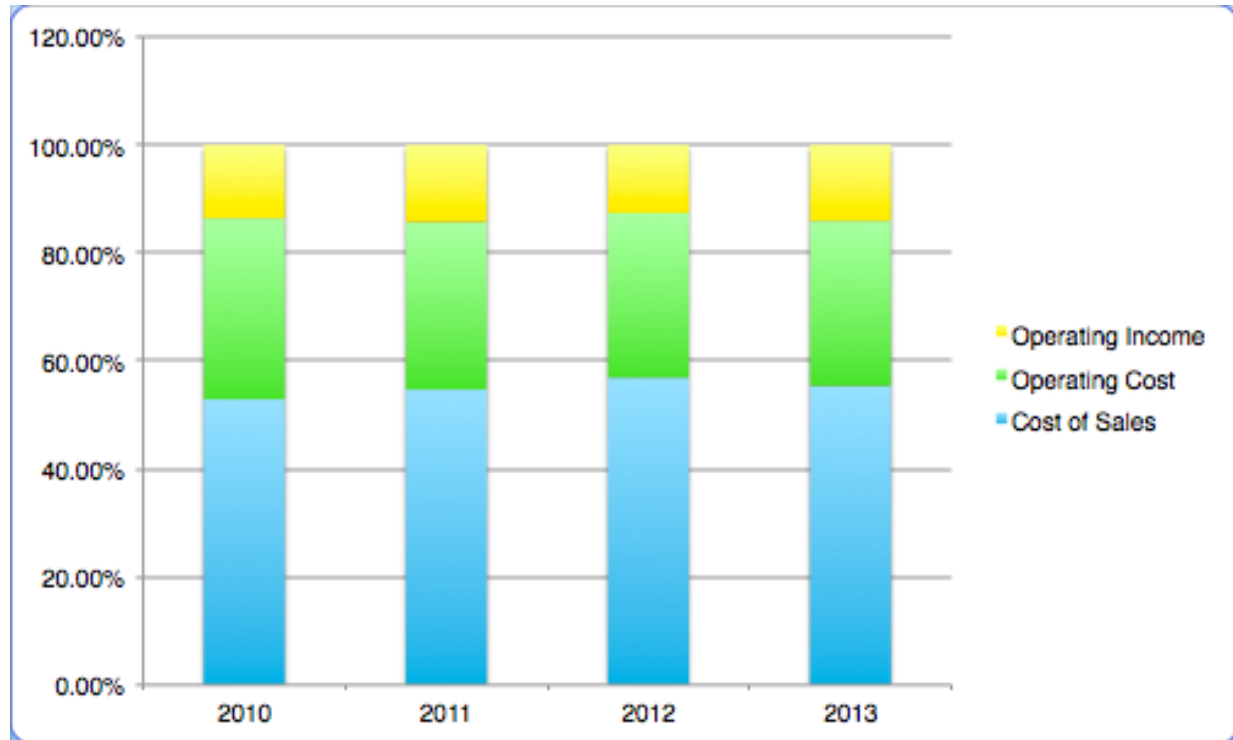
(IN MILLION OF EURO)	2010	2011	2012	2013
<b>Revenue</b>	100%	100%	100%	100%
Cost of Sales	52.91%	54.71%	56.91%	55.38%
Gross Profit	47.09%	45.29%	43.09%	44.62%
Operating Cost	33.51%	31.02%	30.49%	30.55%
Operating Income	13.58%	14.27%	12.60%	14.07%
Total Financial Income and Expense	0.32%	0.66%	1.55%	0.28%
Income before Minority Interests and Taxes	13.90%	14.92%	14.15%	14.35%
Tax	2.45%	3.10%	2.52%	2.72%
Income before Minority interests	11.45%	11.82%	11.63%	11.64%
Minority Interests	0.03%	0.04%	0.04%	0.05%
Net Income	11.42%	11.78%	11.59%	11.58%

*Source: Own calculation*

As we said in the previous part, we use this method to calculate the proportion in different activities and compare them, we calculate via the formula (2.4), and we can see at last the total revenue is 1. There is one point we need to know that the operating income equals to the income before minority interests and taxes minus total financial income and expense.

So we use the results from the table 4.3 and make a chart to compare them and find the changes between different activities.

**Chart 4.3 Common-Size Analysis of Income Statement**



*Source: Own calculation*

We can see from the table and chart that from the 2010 to 2012, the cost of sales is increasing and the gross profit is decreasing. From the 2012 to 2013, the cost of sales is decreasing and the gross profit is increasing. It shows the trend is Ikea Company are trying to decrease the sale of cost, they are always looking for smart ways to save on costs and optimizing the value chain so they can increase the gross profit and the total revenue. Also we can make this conclusion from other data in income statement, from 2010 to 2013, the operating cost is decreasing, the operating income is increasing. We can generally see that the net income of IKEA Company is increasing, the revenue keeps increased. The percentage of cost of sales is increasing because of the expanding of its market scale, so they need to invest money in it, so the cost increased.

As we know that Ikea Company is a worldwide furnishing company, the most important part is selling their furnishing products and making their profit maximization. Their managers want to increase sales and profits, they are always looking for smart ways to save on costs, they explore every aspect of the product and consider about how to improve its practical applicability and

make it more affordable for everyone, all IKEA group markets from the stores to distribution centers, they were trying to lower their costs by kinds of innovations in products and raw materials. So we can see from the chart that the trend is the cost in decreasing and the profit is increasing.

## 4.2 Trend Analysis

In this part, we will describe the two main financial statements by using trend analysis.

### 4.2.1 Trend analysis of balance sheet

In this part, we use the trend analysis to analyze the balance sheet of IKEA, we can see the changes of the important factors in balance sheet.

**Table 4.4 Data for trend analysis from balance sheet (in millions of Euro)**

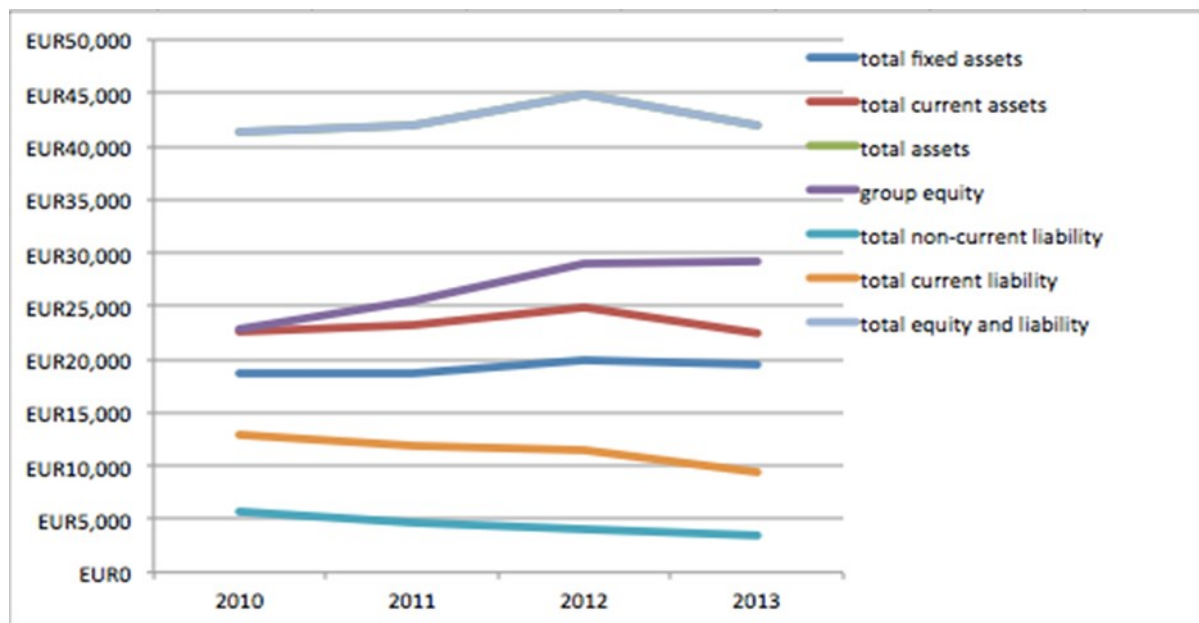
	2010	2011	2012	2013
Total fixed assets	18,665	18,589	19,936	19,529
Total current assets	22,608	23,292	24,812	22,450
Total assets	41,273	41,881	44,748	41,979
Group equity	22,841	25,411	29,072	29,202
Total non-current liability	5,621	4,592	4,148	3,465
Total current liability	12,811	11,878	11,528	9,312
Total equity and liability	41,273	41,881	44,748	41,979

*Source: Own calculation*

We use the trend analysis in this table, we even do not need to calculate anything, we only show the information which provided in the balance sheet. Here we list typical activities in the balance sheet.

So next we use this information to make a chart in the following and we can simply find the change and spot its trend during this period.

**Chart 4.4 Trend Analysis of balance sheet (in million of Euro)**



*Source: Own calculation*

We can see from the table and chart that the total assets is increasing from 2010 to 2012, but decreased during 2012 to 2013, the reason of increasing is that IKEA expand its new stores, warehouses, factories and shopping centers, the reason of decreasing is in order to maintain good service level, so IKEA decrease their inventory. The group equity was increased. As a worldwide company, Ikea expand its business all over the world, the scale of business is becoming bigger. Also, Ikea has its unique way of management structure, so they can control the group equity well and ensure the balance between equity and liability.

#### **4.2.2 Trend Analysis of income statement**

In this part we use trend analysis to describe its financial condition from income statement of Ikea company and shows how much the revenue has the company made during these period.

**Table 4.5 Data for trend analysis from income statement (in millions of Euro)**

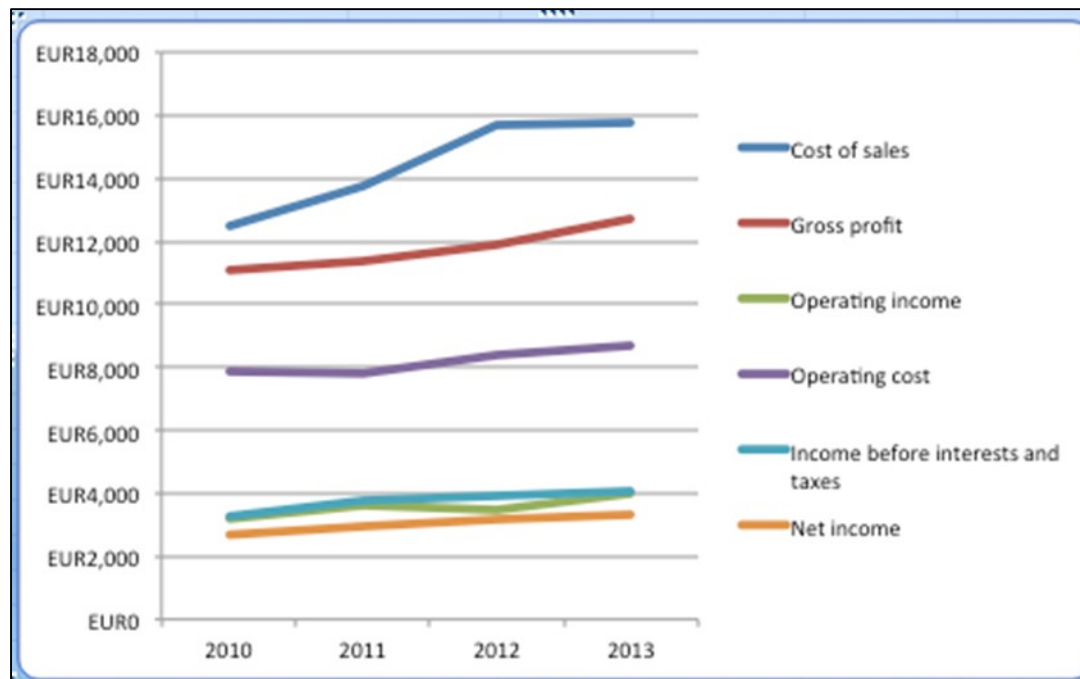
	2010	2011	2012	2013
Cost of sales	12,454	13,773	15,723	15,786
Gross profit	11,085	11,400	11,905	12,720
Operating income	3,197	3,592	3,482	4,011
Operating cost	7,888	7,808	8,423	8,709
Income before interests and taxes	3,273	3,757	3,909	4,092
Net income	2,688	2,966	3,202	3,302

*Source: Own calculation*

We use this method based on the income statement, we do not need to calculate, and we only use the original data from the income statement and choose the typical activities in it.

So then we use the information from the previous table to make the following chart to analysis the trend of it.

**Chart 4.5 Trend Analysis of income statement**



*Source: Own calculation*

We can see from the table and chart that all the factors are increasing, like cost of sales, gross profit, we know that the revenue is increasing, it means that the economic scale of Ikea is

expanding, the economic aggregate is becoming bigger so all the factors are increasing, because of its worldwide strategy, as an international company, Ikea need to expand its retail market in the world, so they need more money to do, then the cost of sales is increasing, meanwhile because of its good operation so its gross profit is also increasing. All the factors show the increased trend, it means that Ikea has a good financial condition.

### 4.3 Financial Ratio Analysis

Financial ratio analysis is one of the most important methods in financial analysis, we use the 4 kinds of basic ratios to analysis and assess the financial health of IKEA.

#### 4.3.1 Profitability ratio

It is a ratio that measures the ability to generate the profit from the invested capital in the form of return during a period. It shows how much profit that the company earns and influence its competitive in the market, it also reflect the quality level of its management. Generally, the higher the profitability ratios are, the better competition of the company is.

The individual calculations of profitability ratios from 2010 to 2013 we can use are in the table 4.6.

**Table 4.6 Profitability ratios**

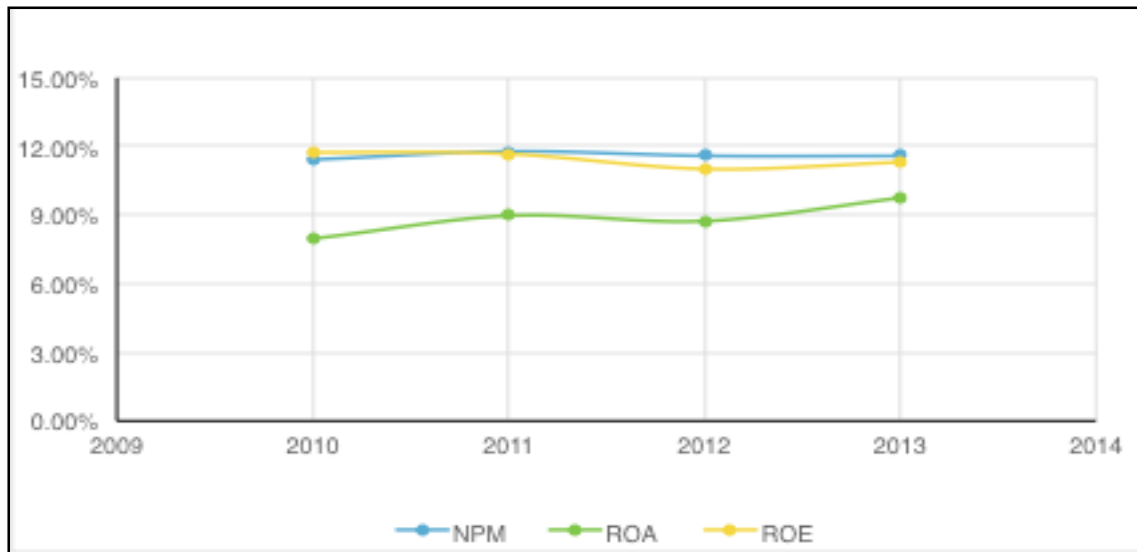
<b>Profitability ratios</b>	2010	2011	2012	2013
<i>NPM</i>	11.42%	11.78%	11.59%	11.58%
<i>ROA</i>	7.93%	8.97%	8.74%	9.75%
<i>ROE</i>	11.77%	11.67%	11.01%	11.31%

*Source: Own Calculation*

In this table, the *NPM* is calculated via the formula (2.6), the *ROA* is calculated via the formula (2.7), the *ROE* is calculated via the formula (2.8).

The development of individual ratios is shown in the following chart, we can find the changes and compare the changes with them.

**Chart 4.6 profitability ratios**



*Source: Own calculation*

So we can see from the table and chart that the *NPM* and *ROE* of IKEA is stable, there is only a little change nearly 1%, it is because the change is similar within these three parts including earning after tax, revenue, and equity during this period, then so the *NPM* and *ROE* only has a little change, about *NPM*, we see that the change is small within 4%, as we can see in the table 4.3 that different changes of net income during the period is same with the *NPM*, from 2010 to 2011, it increased because of relatively decreased of operating cost, lower the cost is always their aim; from 2011 to 2013, the percentage is decreasing because of actively of other financial activities in the company, the change is very small, but the percentage of *NPM* in 2013 is bigger than 2010, the net profit is increasing. About *ROE*, the change is also very small within 0.8%, the trend of *ROE* is decreasing, it states that the changes of equity in four years is bigger than the changes of net profit, the net profit in IKEA is increasing, but the group equity increased more, because IKEA attached much importance to its group equity, we can know from its special business structure, so in this period, not only did IKEA develop their level of net profit, but also IKEA put much effort to develop the group equity and keep the balance with the liability, it shows that the ability in IKEA to raise the money in the market is decreasing a little because of period strategy, but in 2013, the ability is increasing, so it is not a big problem for it. And we see that the change of *ROA* is higher than *ROE*, *ROA* shows the increased trend, the change nearly 2% from 2010 to 2013, it means that the net profit is increasing, and the changes of assets are smaller than net profit, because the ratios are higher and higher during 2010 to 2013, it indicates that the better use of assets in IKEA, because during this period, IKEA was always trying to find a better ways to develop and optimize the value chain in the company.



### 4.3.2 Liquidity Ratios

It measures the company's ability to meet its immediate or short-term liabilities and obligations. The liquidity of a company shows that its ability to have cash available when needed to meet its short-term obligation. We can see the IKEA Company's liquidity ratios in the following table and chart.

**Table 4.7 Liquidity ratios**

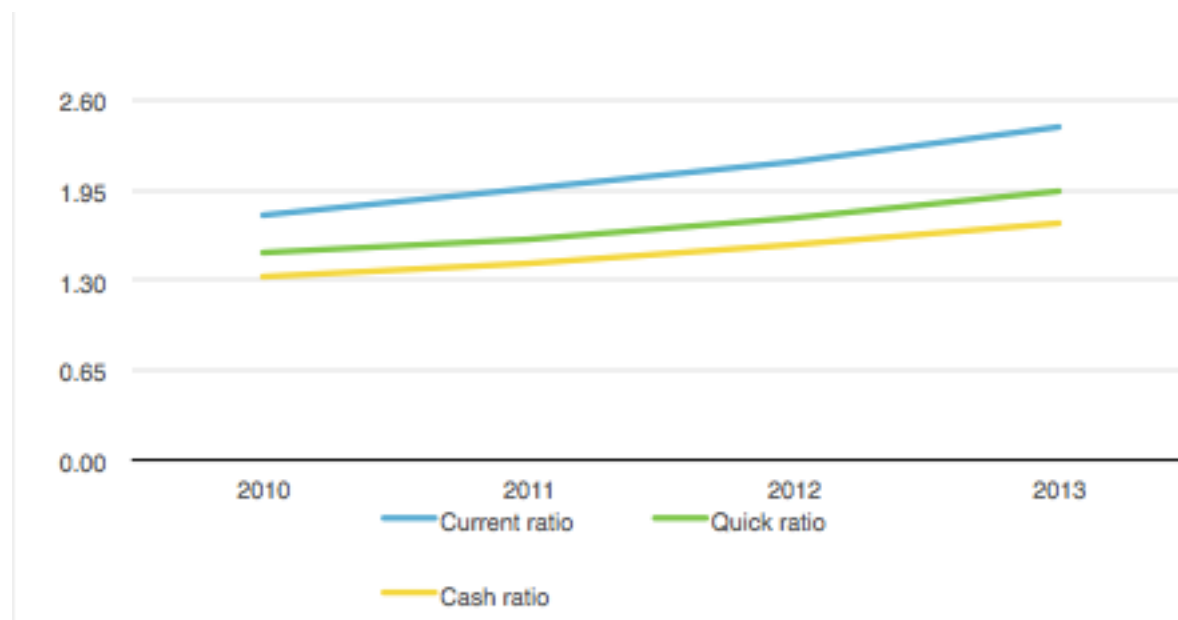
Liquidity ratios	2010	2011	2012	2013
Current ratio	1.76	1.96	2.15	2.41
Quick ratio	1.50	1.59	1.75	1.95
Cash ratio	1.32	1.42	1.55	1.72

*Source: Own Calculation*

In this table, the current ratio is calculated via the formula (2.9), the quick ratio is calculated via formula (2.10), the cash ratio is calculated via the formula (2.11).

The development of these ratios are shown in the following chart and we can find the changes and analysis them.

**Chart 4.7 Liquidity Ratios**



*Source: Own calculation*

There are three main ratios in liquidity ratios. Current ratio measures an amount of current assets for every unit in current liabilities, it shows their relationship, and we can see that IKEA has a high current ratio and it's increasing during 2010 to 2013, it reflects that Ikea is in good financial condition as a worldwide company, and it indicates that IKEA has strong ability to repay its debt, because that the changes in current asset are bigger than the current liabilities. The quick ratio and cash ratio is lower and the difference between these two is not big. The quick ratio test more strictly on company's liability, and we find that the quick ratio is increasing during 2010 to 2013, it indicates that IKEA has strong ability to pay its debt by using cash. Also the cash is increasing too, it shows that the ability of IKEA to repay its current liabilities is stronger. So we can see from that these three ratios are all in increased trend from 2010 to 2013, it shows that the economic development is very well in IKEA, as an international company, IKEA uses full of its money to operate better in their worldwide market, investors like to cooperate and invest with it, so all the liquidity factors are increasing during this period. In this part, we can make a conclusion that IKEA has enough ability to meet its short-term liabilities and obligations, it has good financial condition.

#### 4.3.3 Solvency Ratios

Solvency ratios measure the company's ability to meet its long-term obligations, it shows how the company is financed. We can simply see its result in the following table and chart and analysis it. The formula is based the description of chapter 2.

**Table 4.8 Solvency ratios**

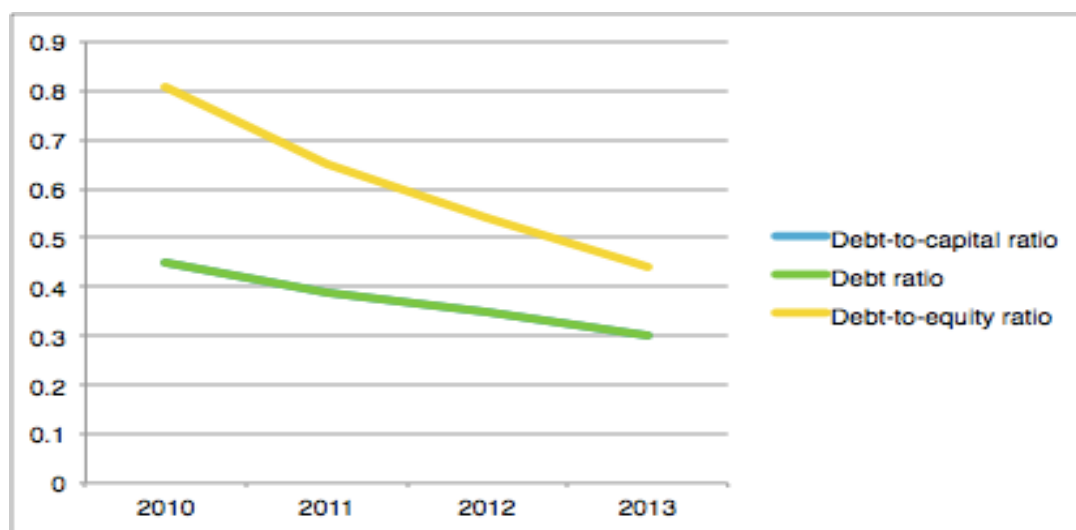
Solvency ratio	2010	2011	2012	2013
Debt-to-capital ratio	0.45	0.39	0.35	0.3
Debt ratio	0.45	0.39	0.35	0.3
Debt-to-equity ratio	0.81	0.65	0.54	0.44
Interest ratio	409.125	375.7	325.75	272.8

*Source: Own calculation*

In this part, the debt-to-capital ratio is calculated via the formula (2.13), the debt ratio is calculated via the formula (2.12), the debt-to-equity ratio is calculated via the formula (2.14), the interest ratio is calculated via the formula (2.15).

So next we find its development in the following chart, we can simply see the changes and trends and analyze them.

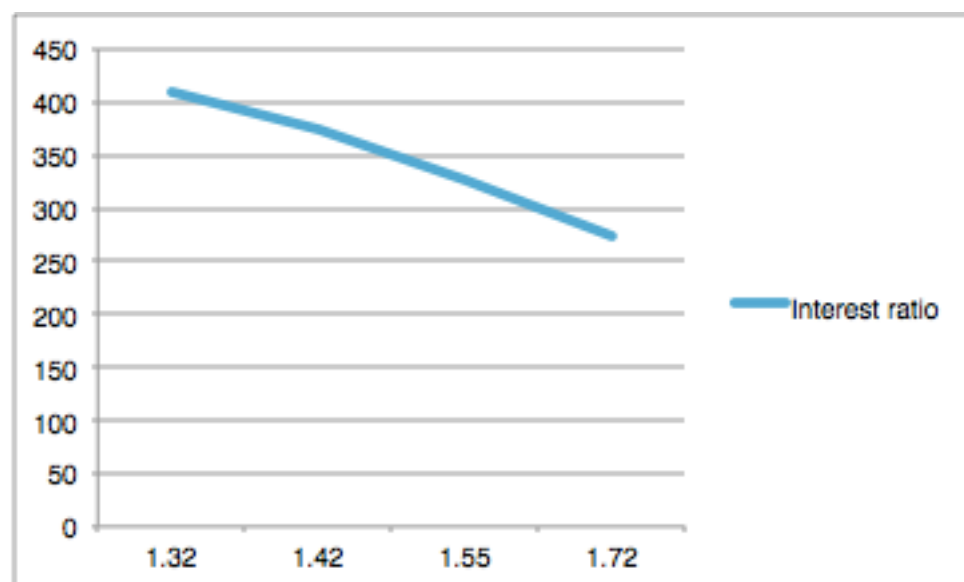
**Chart 4.8 Solvency ratios**



*Source: Own calculation*

Because the distinguish between interest ratio and other ratios are big, so we make a single chart for interest ratio.

**Chart 4.9 Interest ratio**



*Source: Own calculation*

Debt-to-capital ratios measure the amount of total capital financed with debt, debt-to-equity ratios measure the amount of company's debt relative to company's equity. We can see that from 2010 to 2013, all the factors are in decreased trend, it is very obvious, it states that the debt in

company is decreasing and the company has stronger ability to pay back the debt, there is also another condition that the company use various ways in financing and increase their inventories, so their total assets increased. About the debt ratio, it is same with the debt-to-capital ratio, usually the lower the ratio, the less leveraged the company and the less its financial risk, so we can find that during 2010 to 2013, this ratio is decreasing, so we know that IKEA has stronger ability to meet its obligations on the debt. About the debt-to-equity ratio, the relationship is the same, and it is decreasing too, but compared to the debt ratio, the debt-to-equity ratio is higher, it indicates that the company has stronger ability to pay its debt based on assets than the equity. If the debt-to-equity ratio is less than one, so the company doesn't need to use much debt for assets financing than equity. But in general, based on these ratios we know that IKEA has good reputation to deal with its debt because of its good economic development during this period, IKEA is always trying to lower their debt, we can find it in the balance sheet, as a worldwide company, IKEA can fully use their money and keep all the financial activities in balance.

About the interest coverage ratio, it is also decreasing, we can see that this company's operating profit is enough to meet its current interest payments, though the ratio is decreasing, because of the relatively rapidly growth of interests, the amount of earning before interest and tax did not grow up too much compare to the interests, because of expanding business activities of IKEA, so they have to pay more interests than before, it means that the company's financial situation of solvency ratio is not in bad condition, it is fine.

#### **4.3.4 Activity Ratios**

Activity ratios also can be called as asset management ratios, it measures generally are assets are being used, simply called asset utilization. This ratio indicates how well the company uses its assets, it has a direct effect on its liquidity. We calculate the ratios and seen from the following table and chart.

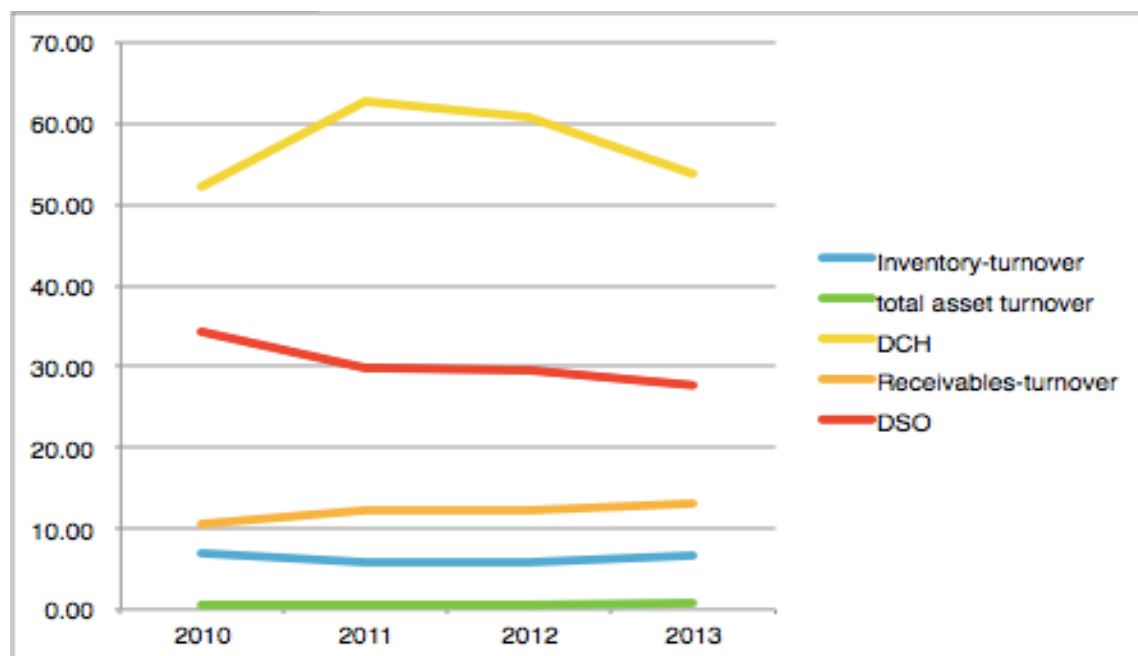
**Table 4.9 Activity ratios**

Activity ratio	2010	2011	2012	2013
Inventory-turnover	6.89	5.74	5.92	6.70
Total asset turnover	0.57	0.60	0.62	0.68
<i>DCH</i>	52.23	62.74	60.77	53.76
Receivables-turnover	10.52	12.12	12.17	13.00
<i>DSO</i>	34.23	29.70	29.58	27.70

Source: Own calculation

In this part, the inventory turnover is calculated via the formula (2.17), the total asset turnover is calculated via the formula (2.19), the receivables turnover is calculated via the formula (2.18), the *DCH* and *DSO* is calculated based on the formula (2.17) and (2.18), we use the number of days to divide them.

So then we use the result of calculation to make the following chart, we can find the changes and analyze them.

**Chart 4.10 Activity ratios**

Source: Own calculation

We can see during these four year that the inventory turnover and total assets turnover didn't have much change, they're relatively stable, it means the company's selling condition is stable. About the inventory turnover, we see from 2011 to 2012, the ratio is lower than 6, because of

the increased of inventory and the cost of sales were always increasing during 2010 to 2013, so in year of 2011 and 2012, so the inventory turnover is lower in 2011 and 2012, because in this period, IKEA increased their expense on inventory, and they need to develop the market and open the new stores, so they need more inventories to support, the reason why the inventory increased in 2013 was that IKEA want to keep their good service level, so they focus more on it in this period, so the inventory turnover increased. About the receivables-turnover, it is increasing from 2010 to 2013, so it means during this period the credit sales increased, also the revenue increased much, the receivables is relatively stable, so the receivables-turnover is increasing, it indicates that IKEA has strong ability to collect its credit sales, the reason is that IKEA has good financial condition, its revenue is always increasing. From 2011-2013, all the factors are increasing which shows the higher turnover of a company. Then about the total asset turnover, it is increasing during 2010 to 2013, it indicates that the company has stronger ability to use the asset successfully to generate the revenues, from the 2010-2013, the assets are relatively stable except 2012, the revenue is always increasing, and the changes are bigger than assets, because IKEA has good financial situation and it operates well, the assets in IKEA can keep stable because it is always trying to keep the balance between different activities in the balance sheet, so using the stable assets to earn more revenues, more revenues give them ability to grow. We can know that Ikea are improving the quality of using their assets. We use the *DCH* and *DSO* to know more changes according to the number of days, the trend is same with the inventory turnover and receivables turnover.

#### 4.4 Pyramidal Decomposition of Ratio Return on Equity

In this chapter, we use the pyramidal decomposition method to analyze the *ROE* ratios. The *ROE* ratio has three parts that includes net profit margin, assets turnover and financial leverage. We can use this method to find out which factors have greater impact on *ROE*. We calculate the result about the relative and absolute change of component ratio in the following table.

**Table 4.10 Relative change of component ratio**

	2010-2011	2011-2012	2012-2013
<i>ROE</i>	-0.85%	-5.66%	2.72%
Net profit margin	3.15%	-1.61%	-0.09%
Asset turnover	5.26%	3.33%	9.68%
Financial leverage	-8.79%	-6.61%	-6.61%

*Source: Own Calculation*

From the table 4.10, we can see that ROE nearly didn't change during 2010-2011 and 2012 to 2013, it only changed about -5.66% during 2011-2012. From 2010-2011, the biggest change is net profit margin and financial leverage, the asset turnover has less influence, and net profit margin is positive and financial leverage is negative, so we find that ROE almost didn't change during this period. From 2011-2013, the net profit margin didn't change, the financial leverage has bigger influence than asset turnover. From 2012 to 2013, the net profit margin is -0.09%, the asset turnover is more positive than financial leverage, so *ROE* is positive, it is due to the better use of asset turnover.

Following table is about the absolute change of component ratio on *ROE*, we can see the trend of component ratios from it and whether is in same trend or in opposite on *ROE*.

**Table 4.11 Absolute change of component ratio**

	2010-2011	2011-2012	2012-2013
<i>ROE</i>	-0.10%	-0.66%	0.29%
Net profit margin	0.36%	-0.19%	-0.01%
Asset turnover	3.00%	2.00%	6.00%
Financial leverage	-15.88%	-10.89%	-10.17%

*Source: Own calculation*

We can see that the net profit margin increased during 2010-2011, decreased during 2011-2012 and 2012-2013, the asset turnover is increasing during 2010-2013, and the financial leverage is decreasing during 2010-2013. So we find how trend of these component ratios, we will analysis relative and absolute change of component ratios in the following chapter by three methods including gradual changes method, logarithmic decomposition method and functional decomposition method.

#### 4.4.1 Method of gradual changes

We use the method of gradual changes and the results and trend of component ratios are in the following table and chart 4.12.

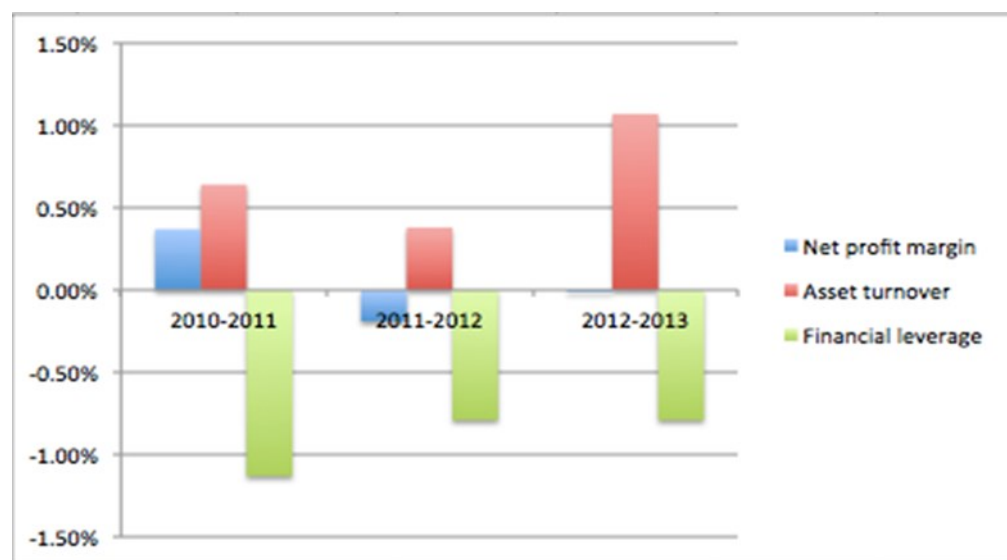
**Table 4.12 Component ratio on *ROE***

	2010-2011	2011-2012	2012-2013
Net profit margin	0.37%	-0.19%	-0.01%
Asset turnover	0.64%	0.38%	1.07%
Financial leverage	-1.13%	-0.79%	-0.79%

*Source: Own calculation*

In this part, we use the formula (2.26) to calculate these three components. Then we use the data to make the following chart to find out the changes and which has the biggest influence on *ROE*.

**Chart 4.11 Component ratio on *ROE***



*Source: Own calculation*

So we can see that during 2010-2011, asset turnover has the greatest influence on *ROE*, then is net profit margin, the financial leverage is negative. Also during 2011-2013, we can find that asset turnover always has positive impact on *ROE*, then is net profit margin, the last is financial leverage, it has negative impact on *ROE*, the proportion of influence from these three component are different, it means that the use of asset turnover is the main factor that influence the *ROE* in this period.

The asset turnover always show as the important factors on *ROE* from 2010-2013, whatever in relative or in absolute change, it has positive change during these years. It is the biggest factor during 2012 to 2013. We can also see during 2012-2013 from the annual report that the IKEA expand its market in the world, their economic aggregate is increasing, and their revenue and asset is increasing, so the asset turnover is increasing. The reason that the revenue was increasing was the good management and right marketing decision made by IKEA, also the costs were decreasing.



The financial leverage always has negative impact on *ROE* during 2010-2013, because in relative or in absolute change, the value of number is negative. But it is the biggest factor during 2010 to 2012. Because the IKEA was increasing their equity and decreasing their liability, so the ratios always decline during these years, especially during 2010 to 2012 compared with the asset turnover, it had greater influence on *ROE*, but it also showed that IKEA had a good financial development during these years, it kept a good balance between liability and equity.

#### 4.4.2 Method of logarithmic decomposition

In this part we will use method of logarithmic decomposition, it's also one of the ways to compare which is the biggest factors that influence *ROE*.

**Table 4.13 Component ratio on *ROE***

	2010-2011	2011-2012	2012-2013
Net profit margin	0.35%	-0.23%	-0.01%
Asset turnover	0.57%	0.34%	1.03%
Financial leverage	-1.11%	-0.82%	-0.75%

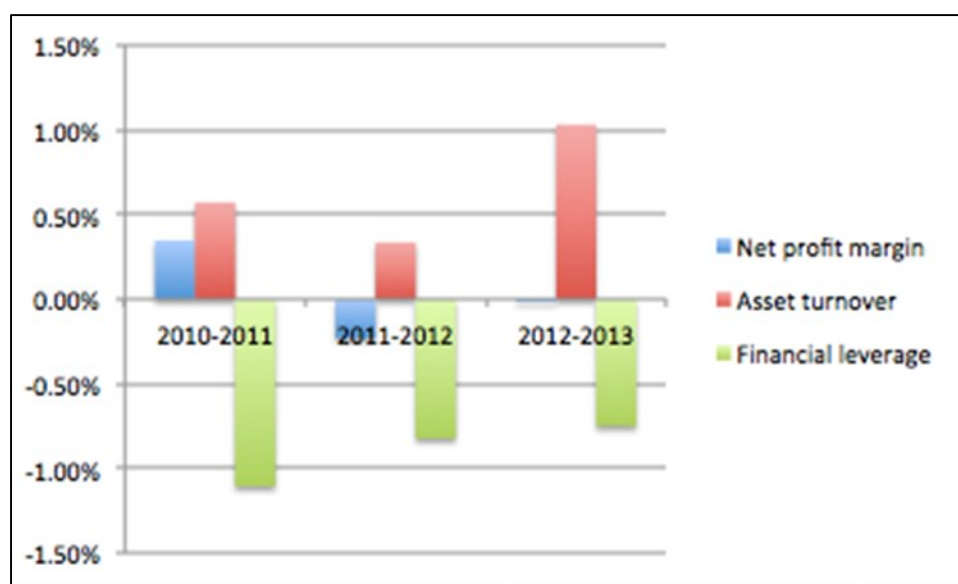
*Source: Own calculation*

So in this part, we use the formula (2.27) to calculate these three components.

From the table 4.13 we can see that the calculation result is similar to the gradual changes method, the most biggest influence factor on *ROE* is financial leverage during 2010 to 2012, and asset turnover during 2012 to 2013. From 2010-2011, asset turnover and net profit margin has positive impact on *ROE*, the financial leverage is in negative. From 2011-2013, the asset turnover has positive influence on *ROE* while net profit margin and financial leverage all has negative influence. About the details we already introduced in the gradual method.

So then we make the following chart based on the previous table to find out the changes and which has the biggest influence on *ROE*.

**Chart 4.12 Component ratio on *ROE***



*Source: Own calculation*

From the table 4.13 we can see that the calculation result is similar to the gradual changes method, the most biggest influence factor on *ROE* is financial leverage during 2010 to 2012, and asset turnover during 2012 to 2013. From 2010-2011, asset turnover and net profit margin has positive impact on *ROE*, the financial leverage is in negative. From 2011-2013, the asset turnover has positive influence on *ROE* while net profit margin and financial leverage all has negative influence. About the details we have already introduced in the gradual method.

#### **4.4.3 Method of functional decomposition**

In this part we use this new method of functional decomposition. It's also one of the methods to calculate the decomposition of *ROE*.

**Table 4.14 Component ratio on *ROE***

	2010-2011	2011-2012	2012-2013
Net profit margin	0.36%	-0.18%	-0.01%
Asset turnover	0.60%	0.37%	1.51%
Financial leverage	-1.08%	-0.78%	-0.74%

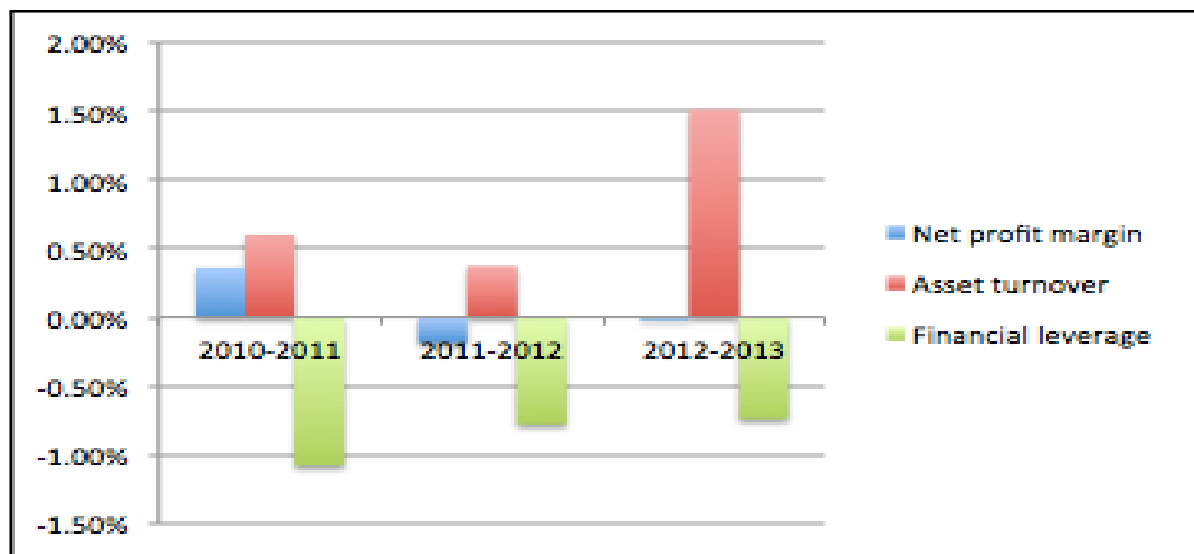
*Source: Own calculation*

In this part, we use the formula (2.28) and (2.29) to calculate these three components.

We can make a same conclusion from this table and chart that the calculation result is similar to the gradual changes method and the logarithmic decomposition method. About the details we already introduced in the gradual method.

Then we make the following chart based on the previous table to find out the changes and which has the biggest influence on *ROE*.

**Chart 4.13 Component ratio on *ROE***



*Source: Own calculation*

From the table 4.14 we can see that the calculation result is similar to the gradual changes method and method of logarithmic decomposition. The most biggest influence factor on *ROE* is financial leverage during 2010 to 2012, and asset turnover during 2012 to 2013. From 2010-2011, asset turnover and net profit margin has positive impact on *ROE*, the financial leverage is in negative. From 2011-2013, the asset turnover has positive influence on *ROE* while net profit margin and financial leverage all has negative influence. About the details we have already discussed in the first method.

## 5 Conclusion

It is the final part of the thesis, we have already introduced the profile of IKEA Company, described the basic financial analysis methodology and put it into practice, we used the common size analysis, trend analysis, financial ratios analysis and the pyramidal decomposition analysis in the fourth part, now we can make some conclusions.

The goal of submitted bachelor thesis is to assess the financial performance of IKEA Company during 2010 to 2013 periods.

Firstly, at the aspect of the profitability ratios, we see especially that the ratio of return on asset was increasing during 2010 to 2013. IKEA Company as the biggest furnishing company in the world, the globalization is their business strategy, the owner had this vision since IKEA was firstly established, also they have to be globalization, after the financial crisis in 2008, the whole market is not flourishing enough, they need to find new potential market and find the materials suppliers who can provide lower price in order to lower the cost, so they are always finding appropriate opportunities to open its new branches in the world, they need to use full of its assets, also we find that the revenue is always increasing during this period, the company got the positive profits from 2010 to 2013. So we can make a conclusion that IKEA Company has a good profitability, their net profit margin and return on equity was stable in this period, based on the return on asset we know that IKEA use full of its assets, the amount of assets didn't change much during this period, meanwhile it earned more profit, so its profitability level is in good condition.

Secondly, according to the liquidity ratios, the three main ratios include current ratio, quick ratio and cash ratio were all increasing during 2010 to 2013, they reflect that IKEA Company has strong ability to meet its immediate or short term liabilities and obligations, their liquid assets can be quickly converted into cash. We see that the basic trend of total current assets were increasing, the total current liability was decreasing during this period. IKEA expand its market in the world, so they need to collect much fund and buy the inventories in order to develop, because of its unique business structure, IKEA has a strict way of collecting fund, the INGKA Holding control the inflows and outflow of IKEA, they have responsibility to control the amount of liability, the growth of earning is bigger than liability, so the total current liability

is decreasing. We can make conclusion that IKEA Company doesn't have the liquidity problem of funds.

Thirdly, according to the solvency ratios, the three main ratios include debt ratio, debt to equity ratio and the interest ratio were decreasing during 2010 to 2013, they indicate that IKEA Company has the small risk of being default, it has strong ability to pay back its long term obligations. We know that the trend of total liquidities were decreasing, within these three ratios, the biggest change is on the debt to equity ratio, because during 2010 to 2013 the group equity increased much especially during 2010 to 2012, after the financial crisis in 2008, many companies were closed because they didn't have ability to keep the balance between equity and liability, the proportion of liability was too big so that they can not pay back. IKEA has its special department to deal with them, they controlled the amount of liabilities and increased the percentage of equity. We can make a conclusion that IKEA doesn't have problems to repay its long-term debt, it has good credit reputation.

Fourthly, according to the activity ratios, it can also be called the utilization of asset. We especially focus on that the total asset turnover and receivables turnover were increasing which shown that IKEA Company has strong ability to use assets to generate revenue and its credit sales. During 2010 to 2013, the reason is similar to the profitability, IKEA use its relatively stable assets to earn much more revenues, and meanwhile, IKEA uses the profit to have a greater growth. IKEA was always finding chances to make progress, it seized the opportunities to invest and received later. We can make a conclusion that IKEA use pretty well on using its assets, it has a good behavior in the business market.

Finally, according to the pyramidal decomposition ratio about return on equity, we use this method to measure which components connected with ROE has the biggest influence on it. We can simply find that the biggest factor is financial leverage during 2010 to 2012, and asset turnover during 2012 to 2013. They are the two main factors that influence ROE. The revenues and equity had great changes during this period with relatively stable total assets. Because of IKEA's good management, the costs were decreasing and the revenues were increasing. We can make a conclusion about *ROE* that if the IKEA Company wants to generate more profits from every unit of owners' equity, they should focus on more about its activity ratio and solvency ratio to keep them in healthy condition.

So in conclusion, IKEA Company has a great future, it shows a good result according to the financial analysis. For IKEA, lower the cost and ensure the quality are always their tasks, it is important for IKEA to make right marketing decisions to earn more profits so they can make greater progress. IKEA has a great potential not only in the countries where it already had stores but also in where it does not have any stores, so there still be much spaces for it to develop. As a furnishing company, no company can replace its efficient operation system in the world, and it maintains the agency which has high efficiency and low cost of the business value chain, not only does it sell the products, but also it express the attitude towards life. Based on the aim of this thesis, IKEA company shows a good financial situation during 2010 to 2013, as a business company, it is qualified and there still be a long way for it to walk through, it is worthy for other companies to learn.

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## List of Abbreviations

*A*: Assets

*ACP*: Average collection period

*C*: Cost

*E*: Equities

*EAT*: Earning after tax

*EBT*: Earning before tax

*I*: Income

*IT*: Inventory turnover

*L*: Liabilities

*NPM*: Net profit margin

*OP*: Operating cost

*OPM*: Operating profit margin

*R*: Revenue

*ROA*: Return on assets

*ROE*: Return on equity

*RT*: Receivable turnover

*T*: Tax

*t*: Tax rate

*TAT*: Total asset turnover



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.....YI CHEN ZHANG.....  
Student's name and surname

## **List of Appendix**

Annex 1 Consolidated balance sheet from 2010 to 2013

Annex 2 Consolidated income statement from 2010 to 2013

## Appendix 1: Consolidated balance sheet from 2010 to 2013

(IN MILLION OF EURO)	2010	2011	2012	2013
Property, plant and equipment	15 982	16 173	17 264	17 036
Other fixed assets	2 683	2 416	2 672	2 493
<b>Total fixed assets</b>	18 665	18 589	19 936	19 529
Inventory	3 415	4 387	4 664	4 257
Receivables	2 238	2 077	2 270	2 193
Cash and Securities	16 955	16 828	17 878	16 000
<b>Total current assets</b>	22 608	23 292	24 812	22 450
<b>Total assets</b>	41 273	41 881	44 748	41 979
<b>Group equity</b>	22 841	25 411	29 072	29 202
Long-term liabilities	4 296	3 123	2 523	1 898
Other non-current liabilities	1 325	1 469	1 625	1 567
<b>Total non-current liabilities</b>	5 621	4 592	4 148	3 465
Short-term liabilities	7 724	7 107	6 814	4 763
Other payables	5 087	4 771	4 714	4 549
<b>Total current liabilities</b>	12 811	11 878	11 528	9 312
<b>Total equity and liabilities</b>	41 273	41 881	44 748	41 979

**Appendix 2: Consolidated income statement from 2010 to 2013**

(IN MILLION OF EURO)	2010	2011	2012	2013
<b>Revenue</b>	23 539	25 173	27 628	28 506
Cost of Sales	12 454	13 773	15 723	15 786
Gross Profit	11 085	11 400	11 905	12 720
Operating Cost	7 888	7 808	8 423	8 709
Operating Income	3 197	3 592	3 482	4 011
Total Financial Income and Expense	76	165	427	81
Income before Minority Interests and Taxes	3 273	3 757	3 909	4 092
Tax	577	781	695	775
Income before Minority interests	2 696	2 976	3 214	3 317
Minority Interests	8	10	12	15
Net Income	2 688	2 966	3 202	3 302